How to Forecast Business and Investment Conditions

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How to Forecast Business and Investment Conditions

By Frank Crowell

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Introduction

The claim of this book to the attention of the business man and the investor lies chiefly in the broad experience and careful observation of the author during an active and successful business career covering nearly forty years.

While he has not neglected the theoretical studies of economists, he has in the main relied upon his own knowledge, reasoning and observation; and he now makes the results public for the benefit of others.

In editing the book, I have been continually surprised at the clearness and simplicity with which he traces the history of the typical trade cycle from year to year and I do not see how his work can fail to be of the greatest interest and value to investors and business men. It is, in fact, a real "key to financial success," for those who will read it carefully and use it.

It may be well to mention here that the author is far from claiming any ironclad law of periodicity in the twenty year cycle. It should be obvious that the period may be somewhat lengthened or shortened by current events, but the general operation of the cyclical law remains substantially uniform.

G. C. SELDEN.

Preface

I have endeavored to make this work as easy as possible to comprehend, omitting all abstruse reasoning and technical terms.

I started collecting my notes with no idea of publishing them, and changed my mind toward the last, so that there may be several quotations incorporated in the work that I would have been pleased to give the author credit for, but it is too late to attempt to identify them. Occasionally, I repeat advisedly, where I wish to bring out a fundamental principle and impress it on the reader.

I wish to acknowledge my indebtedness to the following writers on economics: C. D. Wright, author "Alphabet of Finance"; Carroll, "Principles of Finance"; G. F. Johnson, S. Leavitt, William Gibson, William Burton, W. B. Jones on "Economic Crises"; Conant, Jevons, Mills, Juglar, Prof. Norton, and especially to Theodore Burton.

My dates at the head of chapters are necessarily approximate, but will be found to be very close, so far as the past is concerned. The reader can easily allow for any small discrepancy in point of time. Most of my references to "commercial panics" refer to 1873 or 1893.

FRANK CROWELL.

New York City,
July 1, 1910.

I.—Some Fundamental Conceptions

AT first might was right; later barter was evolved.—In the very early stages of man's existence as the cave dweller he undoubtedly took what he desired by right of might or by stealth. Later on began tribal relations and barter sprang up among the members of the tribe only; a simple transfer at first of one article for another. In order to barter, however, they had first to agree on values; and labor was finally recognized as the chief basis of value.

Division of labor.—Later, as the tribe increased in numbers, a division of labor took place and those who were not equal to fighting manufactured for the tribe; thus the factory began in the home. As the workers became more expert and manufactured more than was needed, there sprang up a pressing need of some medium of exchange whereby unequal things could be bartered, and also to enable the manufacturer to store up the results of his surplus labor in the form of some object of general desire, that he could convert later on into whatever he then wanted.

Gold the chosen medium of exchange.—As long as barter was confined to the tribe, some convenient object of general desire having an inherent value

recognized by all, was utilized; but as this intercourse extended to other tribes it became necessary to have some common medium of exchange. Metals were found to have an intrinsic value, were easily portable, indestructible and divisible. Finally gold was adopted as the best medium of exchange. Its value was at first established entirely by demand and supply. Later on the king or government assumed the sole right to coin money. Money, therefore, is the accepted tool of exchange—a merchandise with a special character.*

Paper money introduced.—As business increased the amount of gold coined was insufficient for the requirements of exchange. Gold was also too bulky for large transactions; and credit money, in the shape of paper, was issued by the Government.

Credit.—When the world had become desirous of extending business operations, and sufficiently civilized to regard the sanctity of a promise and to enforce it by law, credit was introduced into business transactions. The owner parted with the goods and accepted the purchaser's promise to pay in lieu thereof. Also notes, bills of exchange and checks were introduced, expressive of the growing confidence in business circles, and because even money became too cumbersome as business transactions increased.

Laborer paid in kind.—Before money was originated the laborer was paid in kind, and this kept him a vassal to his feudal lord, but the use of money allowed the laborer to wander from place to place and finally made a free man of him. Gradually this enabled the lord to dispose of the products

* Compare Carroll's Principles of Finance; also Alphabet of Finance.

of his soil to other than his followers, opening up for the first time a market for his surplus.

Broker first; later became banker.—As money began to circulate widely the different kinds became difficult to equalize and the money broker was evolved—one whose business it was to act as a go-between. Exchanging monies was his principal business; but later, as the supply of money increased and it came into general use, he naturally became the depository of this money, then loaned it, and so evolved into a banker. But in America it was as late as the dawn of the nineteenth century before the people felt reasonably safe in placing their savings out of their own control in the hands of bankers.

Man's utilization of power affected business greatly.—As long as man's motive power consisted only of manual labor supplemented by animals, and later by the windmill, his producing capacity was very small and his business transactions of a primitive order. This continued as late as one hundred years ago, when steam was discovered, furnishing cheap power. Steam, however, was not generally utilized until between 1850 and 1865. It made possible, from that time forward, our steamboats, railroads and great manufacturing capacity; to be supplemented later on by the discovery of electricity. These factors, increasing the volume of business so enormously, both made necessary and formed the foundation of modern business methods, the keynote of which is systematic distribution.

Old panics caused by drouth and famine.—It was famine conditions, superinduced by war, drouth, or floods, that created panics in olden times, but by the aid of the railroad, the steamboat and modern

business methods, famines have been practically abolished among civilized nations.

Former panics destroyed values.—The old time panic resulted from actual destruction of goods, whereas our modern panics create a derangement of the country's industries for the time being, with but a small percentage of actual destruction.

Modern panics of recent origin.—Our best writers agree that modern panics are of very recent origin and have their chief basis in our credit system, which at times is inadequate to meet the requirements of our vast and increasing production. This is the very reverse of the failing supplies of former times.*

Birth of corporations.—The birth of modern corporations was in response to an increasing supply of wealth among the masses, demanding an investment outlet. By means of corporations the people were able to become interested in great business undertakings.

Effect of corporations.—The corporation, with its aggregation of capital, and with a wide market for its shares, gave to many properties and enterprises a mobility and divisibility which greatly facilitated their management. To this great step forward in business organization we owe our modern banks, life insurance and trust companies, canals, railroads, etc.

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*See Prof. Newrath in *Economic Review*, v. 17, p. 28. Jones, Economic Crises, pp. 1-8, says: "The crisis is practically of nineteenth century origin." Also see First Annual Report of the Commissioner of Labor on Industrial Depression, p. 15: "Indeed the economic crisis in its modern form is essentially a phenomenon of the organization of industry and credit." See also Burton, Crises and Depressions. Jones, Economic Crises, says: "The conditions under which crises occurred formerly are so different from those prevailing since, that it may be safely said that little of value can be found in discussions published prior to 1837." See Bolles, Financial History of the U. S., p. 1, 1774-1787.

Practically all the great undertakings of the last fifty years have been accomplished through corporations.

Periodicity of panics.—Science teaches that "an original impulse of any kind finally resoves itself into periodic or systemical motion." Working under this law, the periodicity of panics is so marked, especially in the older countries, as to be almost beyond question. The cycles are periods of approximately ten years, with a variance that is ordinarily but slight, due mainly to political events, as a war or a revolution, debasing the currency, or unwise legislation.*

Two kinds of panics.—I divide panics into two main divisions: the securities or financial panic, in which the crisis is the main feature; and the other the general or commercial panic, in which the depression that follows is more severe in its effects than the crisis itself. The former is a stock panic and has sympathetic effect on business. The latter affects all financial, commercial and industrial lines and is altogether a very serious affair. These are

* See Webster's Essays; also Prof. Nicholson, Political Economy, v. 2, pp. 213-214. Gibson, Cycles of Speculation, pp. 24-33, says, "That there has been a recurrence of these troubles (crises) about once in ten years, is not a debatable question." Also Prof. Pareto, Cours d'Economie. Jevons divides crises by almost exactly ten years periods. Burton, Crises, pp.307-308, says: "Periodicity is no accident, as an examination of the rules which govern industrial and commercial movements will show." Also consult Walter Bagehot; and Jones, Economic Crises, pp. 1-22. Frederick Engels, Socialism, pp. 64-65, says: "The world's industrial and commercial production and exchange are thrown out of joint about once every ten years." First Annual Report of Commissioner of Labor on Industrial Depression, p. 15, says: "The features of regularity and contemporaneousness of crises and depressions have been apparent since the commencement of the century." Consult Conant, *Yale Review*, v. 9, p. 386. Mill divides the ten years between panics into three periods. Edmond Therey in *N. Y. Times*, Jan. 20, 1910, says: "The law of periodicity of crises being clearly established," etc. See Selden, Trade Cycles, in *Quar. Jour. of Economics*, v. 16.

both periodical. It takes each about twenty years to culminate and readjust values. One occurs every alternate ten years, so that the two occur in each twenty year cycle and can be thereafter fairly accurately forecasted unless delayed or expedited by war or some other influence of vast economic importance.

A third but minor division would include incidental crashes or flurries occurring from time to time, which are the result of temporary causes; such as money stringency, political happenings, unwise currency or other legislation, manipulation in Wall Street, a convulsion of nature, such as an earthquake or great fire, some great failure, etc. Most of these affect only the money and credit market, and have temporary effect on the stock market, more or less severe, but they seldom seriously depress the commerce or industries of the country. They are mostly of short duration and usually cause only a temporary displacement of values.

Securities panic.—The securities panic is preceded by a long period of liquidation in stocks, generally of two or three years duration, and is followed by stagnation on the stock exchange for a year or more thereafter, a readjustment of stock values and a reflex effect in business lines.

Commercial panic.—The commercial or business panic is preceded and followed by several years of liquidation, causing great losses and wages and price reductions and affecting all values. The period of readjustment covers several years.

Greatest of minor panics.—The greatest of the minor panics, so called, comes at the termination of the great rise in stock and commodity prices during a boom period. When the strain of money and

credit from the pressure of the great volume of business done in all lines is too great, a crisis occurs, and if at this time the element of fear as to the stability of financial institutions is introduced, it may beget a stringency panic, such as occurred in November, 1907, and was only narrowly avoided in 1887 and 1867. Such a crisis is more serious and lasting, because it comes at a time when the reaction from excessive prices and over-extended credit has naturally set in.

Universality of panics.—As our relations with all other countries grow more intimate, the tendency is toward a uniformity of panic periods. The crisis is merely a natural reaction from a period of excessive extravagance and speculation, which, if continued, would only lead to still worse results. After recovery from every crisis the people live on a higher plane of consumption and enjoyment.

Cause of fall in prices.—Vanishing credit, in time of panic, is the primary cause of the fall of prices. Too often we have resorted to inflation as a means of preventing panic, forgetting that, fundamentally, it is not business that adjusts itself to the volume of money, but money that adjusts itself to the volume of business. Inflation defeats its own purpose by furnishing the speculator with more funds to boom prices with at the very time when the slowing down of business and the decline of prices is the natural and necesssary remedy.

Effect of increased gold output.—The wonderful gold output of late years, the supply increasing much faster in proportion than the increase in population, has stimulated commerce and industry wonderfully and been greatly instrumental in raising prices. The increased gold supply has been brought

about by improved methods of mining, new inventions, and economies in production. Prof. Norton states that from Jan. 1, 1896, to Nov. 1, 1906, our gold output increased 80.7 per cent. and our commodity prices 37.2 per cent. Ten to fifteen years ago, he says, "it did not pay to operate a mine where the average yield of gold was less than $12 per ton; now $1.30 per ton will yield a paying return." It is cheapened production, of gold as of other things, that is most influential in placing man on a higher plane of living and in making the bare necessities of life more easily obtainable.

Effect of modern financial methods.—Modern financial methods, as exemplified in banking in particular, increase greatly the circulation of money, making one dollar do the work that several formerly did, and being practically equivalent to a great increase in money. Especially is this so in the cities, where money will do many times the work that it would do in the wilds of Africa, for instance. Credit also has increased so greatly that in the United States only about 3 per cent. cash is used in the Clearing House and 5 per cent. in banking and business operations; until now credit is the chief medium of exchange and gold is mainly used for reserve purposes and to adjust balances.

Abuse of credit.—Evidently we must be careful of credit in our endeavors to increase the supply of money, the latter representing so small a percentage; and as this credit structure grows, one can easily realize that this small percentage of money must be the best possible, without the shadow of a doubt attached to it, or the whole vast structure will be involved in ruin. Hence mere agitation of the subject is a serious matter. It finds instantane-

ous reflection in the financial world and, if continued, in the commercial and industrial world as well. As credit vanishes its burden of work is shifted to money, but the task is too great and hoarding sets in; prices fall and general liquidation is in order.

The bulk of bank and trust company deposits are not cash but credits—mere bookkeeping entries backed up by the depositors' checks, notes, or securities. National banks in central reserve cities can issue credits equal to four times the amount of their money reserves; and banks in the smaller cities and towns six to twenty times the actual cash in their vaults. In times of great activity credit even exceeds this, because withdrawals of cash decrease the reserve below the legal limits.

Interest.—The true rate of interest is best measured by six months loans on good collateral or by gilt-edged commercial paper, rather than by the rate paid by stocks. Fluctuations in interest rates are often caused by changes in the relative supply of circulating and fixed capital. Interest rates are also affected by rising or falling commodity prices, as such changes increase or decrease the demand for money. The degree of activity in business and on 'change are, of course, factors that affect interest rates.

Prices governed by economic laws.—Prices of securities and commodities are governed by economic laws. The speculator is only an incident, and must work with the law or suffer the consequences. His activities (unless he improves, as by building) cannot create values. All he can do is to hasten the tendency of the times somewhat, or if working against the law, to assist in creating a slight and

temporary displacement of values. His dealings are reflected in the bank clearings, where, however, they cannot be identified, nor do they show his profits or losses. For this reason bank clearings do not tell all the story,* although, generally speaking, they do reflect the volume of business, or of business and speculation combined.

* Burton, Crises, p. 165.

II—Beginning the Twenty Year Cycle

Improving Times. About Three Years after Commercial Panic.

[NOTE—*These conditions last occurred in* 1896. *If the next commercial panic takes place in* 1913, *for example, they may be expected substantially to repeat themselves about* 1916.]

THE reader to forecast coming financial situations.—My desire in the following pages is to trace financial, commercial and industrial development closely from stage to stage during the twenty year cycle (after which period financial history starts in to repeat itself), so that the reader may at any time be able to locate the present status of business affairs, to know in great measure what is before him, understand the laws governing the conditions, prepare himself for what is to come, and thus make timely investments or withdrawals.

We will begin at that period of the depression following a commercial panic when business starts on an ascending scale, with a dawning light of better things to come.

Excesses carry germs of their own destruction.—The extremes of good and bad times have in themselves the elements of their own destruction, for nature abominates an excess. Extreme bad times beget economies and wise management that result in the accumulation of new wealth. This soon causes consumption to outstrip production, and finally requires the employment of more men and the payment of better wages in order to produce enough to satisfy these increased demands.

Country with greatest resources recovers first.—Of two nations that have been equally speculative, the one that has natural resources to fall back on will recover first, for these natural resources constitute a storehouse of wealth that can be drawn upon in bad times; whereas labor is the main asset of the older country, and even this is more or less dependent on the natural products of the younger country to employ it.

Conditions necessary before betterment.—Before any change can take place, not only must overproduction have ceased but the liquidation must be thorough and complete—old debts paid and few new ones contracted, all lines of business on as near a cash basis as practicable, confidence restored in the financial integrity and ability of those we do business with, and above all, a feeling of assurance that prices will go no lower. At this time there will also appear a large excess of exports and low interest rates. All these are indicative of a finished liquidation and a subsequent steady accretion of wealth. Mercantile and financial conditions must have cleared up enough to allow one to do business safely even though on a very small profit.

Farmer and miner feel change first.—It is to the

farmer and miner, those original creators of wealth from the bowels of mother earth, that we must look for the first signs of improvement. By stern necessity driven, we now produce more grains and other farm products than ever before, due to greater care and improved methods being adopted by many, and also to the fact that a large number of persons have been driven to farming as a last resort.

Farmer pays up.—The price for farm products is low, partaking of the tendency of the times, and the export business consequently large; yet gradually the farmer pays his debts and gets on a solid basis, in condition to be greatly benefited by a good crop or two at fair prices, and the accumulation of money, now idle in the banks, forms the basis later for better prices for his products. His crops now generally yield well, for he is working harder and putting more brains into his work than ever before, with consequent good results.

Where crop money goes first.—The returns from these crops go first toward paying up our European indebtedness and liquidating the mortgage obligations of the farmer, later into bank coffers temporarily.

Miner producing gold steadily.—The miners, meanwhile, are busy producing new gold, to be added to the general fund which is accumulating quietly and steadily, in every bank throughout the land. Bank statements reflect the stagnant condition of trade by the steadily increasing percentage of reserves as compared with loans.

Liquid capital must be renewed.—The destruction and diversion of liquid capital was one of the main causes of the commercial panic, consequently this capital has to be replaced and added to before

confidence can be restored. The actual cash in large amounts must be in sight, and interest rates go low enough to render manufacturing profitable, even at the low prices then existing.

Great increase in money depreciates it.—The production of gold has increased during these hard times much faster than the population. This continues until gold is out of proportion to everything else and so depreciates. The foundation is thus laid for a rise in bonds, stocks and commodities; for the only way gold, being the measure of value, can show a depreciation, is through a rise in the articles whose values it measures. As the supply of gold increases its purchasing power grows less.

Some time before increase raises prices.—At first this increasing supply of money is not reflected in the financial world. Hume, Mill and others show that while the volume of money might be increased or diminished instantly, the resulting movement of prices would occur only after an interval when it had time to permeate all the channels of trade.

How an expansion of money with confidence acts.—An expansion of money such as occurs at this time, when confidence is restored, acts as follows: "It first lowers interest rates, then advances prices generally, developing great activity ultimately in business lines, and continues until all of this new supply of money is in active service. Then interest steadily rises, under the stimulus of this growing demand from profits realized, and finally reaches impossible rates and so brings about its own fall." At present, however, it has only reached that stage where it has forced down interest rates to low figures (foreshadowing the great reaction that is to come, for the greater the fall, the greater the re-

bound), and it is now quietly at work stimulating prices for the rise soon to take place.

Growing impatience of owner of idle money.—An early indication at this time is the growing impatience of the money owner with the small yield of his capital in interest returns. This feeling is soon followed by an early stage of returning confidence; then comes a desire to invest.

Stocks and bonds attractive because easily convertible—realty not.—Those investments which are the most easily convertible and from which the quickest results can be obtained, naturally have, if deemed safe, the greatest attraction for the people, especially when, as at this time, investors are so timorous. Hence the attraction of the stock exchange, with its constant action, ready sales and semi-liquid assets, as against real estate with its slow methods, which place it at a great disadvantage, and in bad times, owing to its lack of convertibility, make it an unattractive asset to those who want to realize quickly. It is therefore to the financial world that we must look for any improvement. All great rises depend on the money market; therefore, before any such movement occurs there must be an unusually strong bank showing of available funds on hand.

All wondering why advance does not start in.—At this time every one ~~one~~ is tired out waiting for the change and all are wondering why, with all the material wealth that is being created, the times do not improve; not realizing that this wealth has gone into debt paying and into building up a new supply of liquid capital, to be utilized later in the various business channels when confidence is restored.

Masses timid.—The masses have been frightened

and deeply injured as well in their pocketbooks; they are, therefore, timid and afraid, especially as they are surrrounded with an atmosphere of fear that has its psychological effect on us all. They feel that they can afford to take no risks. Their very financial existence often depends upon a wise investment of their capital, so they intend, if possible, to make no mistakes. Their investments must be readily convertible, so that if afraid at any time they can receive back their cash. They desire to have it in such shape that they can keep posted as to its various rises and falls, so that they can be ready to act at a moment's notice; but, above all, it must be safe.

Bonds are most attractive.—The stock market answers these requirements. At this period stock values seem uncertain, but bonds are a prior lien. Especially attractive are United States, state and municipal bonds, and bonds representing first liens on large corporations that investors know all about.

Safe investments only.—It is investment securities that the people want, and of the safest kind. Their opinion also is strengthened by knowing that the banker who, they realize, is an expert in this line and as a trustee should be careful, has also been quietly purchasing bonds. The banks have found good commercial paper very scarce, business being quiet and money plenty, hence they have sought other investments. So to the bond market we look for the first signs of betterment, indicating a lessened fear, and the quiet birth of an investing movement which, as we shall see, steadily grows as it proceeds.

Poorer classes now buying.—Later, a demand for small denominations of government bonds indicates

that the poorer classes are getting over their fright and are investing, taking their money from hiding places and from the savings banks for that purpose.

Bonds active when interest is low.—The rate of interest yielded by bonds is low, therefore they are most active when interest rates in general are low. This occurs when the business and speculation of the country are quiet, dating from the time business slackens until it starts up again, and until money is in active demand at higher rates than bonds will yield.

Institutions buy bonds.—Institutions have also been buying bonds, as most other securities have been discredited because of the want of confidence and the small amount of business transacted.

Speculator first to buy stocks.—The low rate of interest proves very attractive to the speculator, as at existing prices choice stocks will pay six per cent or perhaps even better, and in large sums he can borrow money of the bank at one, one and one-half, or two per cent. This leaves him a handsome margin. He accordingly buys, rather timidly at first, but more boldly later, as he finds his faith justified and his calculations successful.*

Money goes to Wall Street.—Money must seek an outlet for investment from which it can realize a paying rate of interest, and if mercantile pursuits are dull it generally goes to Wall Street, to be loaned out for investment or speculative purposes. For a time Wall Street is to have a large part of the country's loanable funds at its disposal, and this lays the foundation for a boom in stocks later on.

Banker buys stocks.—The banker, who has heretofore purchased bonds, at length finds that the

* See Burton's Economic Crises, p. 232.

increased demand for these has so raised the price, that their yield is no longer sufficiently remunerative. In the meantime his deposits are growing, and often he is paying interest on the deposits of out-of-town banks. He must have better returns if he is to show satisfactory results to his stockholders, who will hold him accountable. He has watched the Wall Street investor—or speculator, for the operation above described partakes of both investment and speculation. Finding him successful and the outlook now better, fear having in the main subsided and liquidation having ceased, the banker cautiously and advisedly purchases gilt edged stocks. These are now a better investment than formerly, as the general buying of bonds, together with the benefits derived from the successful operations of the farmer and miner, and the increased export trade, are relieving the acute financial conditions of the railroads, and they are paying up their floating debts. This is placing the railroads in a position where they will soon be thinking of spending money in improvements and betterments of road and equipment, which they are now, through long enforced neglect, sadly in need of.

Investors now buying gilt edged stocks.—As investments in bonds increase and values advance, the interest return becomes too small, and investors are driven into the stock market, having confidence that earnings will increase in the near future. They purchase, however, only the gilt edge securities of those large corporations that have been known long and favorably by the public as reliable dividend payers.

Mining stocks bought by professionals.—Mining stocks are in more demand than heretofore among

those whose business it is to buy, sell and develop mines. This is not now a general speculative movement. The public are not in it. It is a quiet absorption by those who are posted on values and are content with a reasonable investment return. Mines are thus developed and the gold output increased, establishing a solid basis for our finances and thereby materially aiding the return of prosperous times.

Farmer and miner have money, which with surplus money in bank, now seeks investment.—The farmer, as we have seen, has paid his debts, and if his crops, with the greater care taken, are now reasonably good, he has money to make purchases on a more extended scale. It is this money and the new wealth from the mines, together with the money going quietly into stocks and bonds, that now begins to show important effects in the commercial and industrial world. Commerce deals chiefly in commodities, which are less readily convertible than bonds and stocks and are therefore slower to move. These markets also must needs apply to the financial world for a portion of that liquid capital which enters into all business operations, and which is now timidly seeking investment. So under normal conditions capital and enterprise seek each other, for the mutual benefit to be derived from the transaction.

Purchasing ability of masses.—At this time the purchasing power of the masses and their disposition to buy are two very important factors, to be studied in their bearing on the business situation.

Low prices for materials encourage the manufacturer.—We will now consider the commercial and industrial sides of business life, to note there, if possible, signs of improvement. Cheap prices for

raw material and labor and low interest rates start up manufacturing. Decreased cost of production often benefits the manufacturer as much as an increase in the price of the finished article, by bringing the product within the purchasing power of a larger number of new buyers and making it more tempting to former buyers, and thus increasing the sales.

Surplus stocks of goods disappearing a good sign.—The first favorable indication, noted some time after the panic, is that surplus stocks on hand are quietly dwindling, due to the diversion of any excess, where possible, to foreign countries, and the restriction of output to meet the demands of the times. Restriction of output, however, is, in nearly every line, merely temporary, and is terminated by a diligent search for foreign buyers, or if the product is not exportable, then finally by growth in population, the quiet gain in the purchasing power of the people, and the betterment in the financial world, with its reflection in all business life.

Consumption outstrips production.—As there is at this time very little inducement for capital to go into production, gradually consumption increases faster than production. Excess stocks first supply these greater requirements but this is only temporary. Requirements must be met later by increased production, and the volume of business then increases decidedly.

New orders first reflect betterment.—Competition must arise between buyers anxious to fill orders before there can be any rise in prices. The first sign of this changing condition of affairs is not found in the clearinghouse returns but in new orders. The former, however, soon follows, and

some time afterwards we find larger loans and a small decrease in the reserve percentage of the banks.

Markets bare and competition sets in.—The increased demand now discloses the fact that certain markets are understocked. The demand is greater than the supply and in the competition that follows prices move slowly upward in those lines first affected.

Capital necessary for a rise.—The first essential condition for a rise is capital. No matter how favorable may be natural conditions, their effectiveness is contingent upon the amount of loanable capital in sight. This great loan fund is most essentially an outgrowth of modern conditions, and has begotten modern financial methods. Banks are merely the reservoirs that contain it.

Other features also necessary for a rise.—Long continued economies practiced by the people result in a large supply of cheaply loanable funds, and these, with good crops, cheap interest, labor and raw materials, cessation of political agitations, the return of confidence (so necessary for future credits) and an underproduction are the advance agents of prosperity. Increase in population and the demand that goes with it is also a very important factor, and hastens the upward movement in those countries that are growing rapidly, giving them an advantage by augmenting their recuperative powers.

Confidence now building up future credits.—Back of all credit, and a fundamental condition for it, is confidence; and this confidence, now quietly generating, is preparing the way for future credits.

III.—Labor Better Employed and Prices Rising

About Four Years After Commercial Panic.

[NOTE—*These conditions last occurred in* 1897. *If the next commercial panic takes place in* 1913, *for example, they may be expected substantially to repeat themselves about* 1917.]

RAILROADS now have funds.—The railroads, once more having a market for their bonds and stocks, and having enforced rigid economies for some time past, are now in a position to make repairs and replace worn out equipment and rails. The work is at first confined, however, to what is strictly necessary, and does not as yet include new extensions. These will come later when profits appear.

Prices of raw materials go up.—The greater demand and competition between buyers to assure early delivery, finally gives the producer an opportunity to charge a higher price—a moderate advance at first, but increasing as he has to pay a greater interest and wage rate, and becoming still greater later on as the necessities of life advance and the pur-

chasing power of the currency, by which the value of his product is measured, decreases.

Manufacturer at first hurt by rise in materials.—This rise in the price of raw materials at first subtracts from the manufacturer's profits, as he is not able at once to raise his own prices correspondingly (coming in competition, as he must, with old stocks on hand) but he does it shortly thereafter as this old supply is exhausted.

Pig iron and copper among first to rise.—Pig iron and copper are raw materials that experience an early rise, entering as they do into the manufacture of so much that is necessary for the daily use of the consumer, and into materials sadly needed at this stage by the railroads of the country, such as structural iron for bridges, rails, electrical supplies, etc. For this reason iron has been called the barometer of trade, and copper might be added of late years, since its uses have expanded so greatly. Lumber and coal rise later and in a less degree. Then follows a gain in cotton goods. These are among the first to rise in the line of manufactured textiles, because they enter so largely into the necessities of both rich and poor.

Betterment reflected in clearings, and buyers increase orders.—The improving conditions are first reflected in the bank clearings of the South and West, the home of raw materials, iron, copper, cotton and food products. All these are basic necessities and the surplusage of them has now been used up. The buyers from these localities, therefore, are the first to increase orders, and this gives a more cheerful aspect to the market.

Many doubt improvement.—There are many doubting Thomases at first who can see no signs of

betterment, because, while our crops are good, there is as yet no large return flow of gold from abroad, and business conditions reflect no marked or obvious betterment; but the money is going into settling our debts at home and abroad, and into paying for securities returned to us from Europe. Many foreign holders of American securities foolishly sell on the first rises in the stock market, to regret it later after conditions have improved, when they buy back at much higher prices.

Prosperity now starts in earnest.—It is when this period of debt paying has passed that prosperity starts in at a surprisingly rapid rate, growing faster all the time; so that even the worst pessimist, whose whole stock of small talk has been the hard times, is finally compelled to abandon it.

Wholesale grocers feel betterment before clothiers.—Wholesale grocers receive larger orders at an early date. They experience the improving conditions before wholesale clothiers, as clothing can be worn when old but food must be replaced. Drygoods do not feel the betterment at first, outside of the increased orders for cotton goods already mentioned.

Human nature wisely optimistic.—The depressed period has now lasted a long time and has been a severe strain on the nerves and pocket books of all of us. Human nature in the main is optimistic. It was wisely made so by the great Intelligence, in order for mankind to look ahead and plan, and first mentally see and then perform the great undertakings which nature is always calling upon us to accomplish in order to better our condition. It is now a time, with basic conditions right and confidence growing, to cast aside the depression of the

past, to look again on the bright side of things and to gather strength for the work before us.

Excess money now loaned and credit started.— The great excess of loanable funds in bank vaults acts as a constant stimulant to speculation, and with growing confidence and improved conditions, money is now loaned more freely and profitably than before, and so helps revive the element of credit, which is later to expand to enormous proportions.

First rise in railroad stocks is based on hopes.— The first advance in railroad stocks, which, as we have seen, precedes the rise in commodities, is always based on hopes of future profits to the railroads, and so anticipates any actual gain. Rapidly diminishing losses at this time are an early indication of the impending rise. The rise in stocks is a sort of reflection of improving conditions in the business world, having as yet no actually tangible basis in profits. It results from a lively appreciation of what is to come and is therefore more or less speculative.

Freight returns better while passenger still poor. —The actual revival in railroad business first appears in increasing freight returns, and when this starts passenger traffic is often making its poorest showing, due to the fact that the people are staying at home, attending strictly to business, and conducting it after the most economical fashion. They are using the mails rather than the railroads to secure new orders, wherever feasible, and traveling for pleasure alone is naturally at a minimum.

Money market gives first signs of improvement.— All changes for the better from time to time, can be early noticed in the money market, for it is here that

all have to come to get the wherewithal to do business with; and the condition of the money market is soon reflected in the stock market.

Railroad dividends often lessened after rise.—For some months after the rise in stocks begins, even prominent railways may reduce their dividends, for those represent, not the present period, but the past six months or year. This fact often temporarily mystifies and disappoints many who had begun to entertain hopes of better things to come.

Rise may take place even when furnace output is decreasing.—Stocks also may rise on 'change, and often do, while the furnace output of iron is still decreasing. This is due, as already explained, to the belief that adverse conditions are changing into favorable ones. The shadow of coming events appears and is acted upon.

Bear failures now.—On this rising market there are apt to be failures of bear operators. For a long time every rise in the market has been followed by a fall, and generally greater than the rise (during the poor times). Many speculators do not yet appreciate the fact that the gain is a permanent one, to be followed by still greater gains. This early rise is much of it manipulative and is financed mostly on borrowed capital.

Public orders first come from outside towns.—The first sign of the general public purchasing stocks appears from out-of-town orders, from localities nearer to the raw materials, where the general business atmosphere is at this time more conducive to optimism than in a large city like New York, which is still suffering from the long continued depression.

Some railroad earnings may even now show losses.—During this period there may be a halt in

the net earnings of some railroads and even a falling off for a short time, with an increased gain later on. This may be due to a severe winter, or strikes, or politics, or, later on, to the more important factor of a rise in wages and commodities that temporarily counterbalances the gain in gross business shown by railroad returns.

Overdo it at first in other lines also.—Moreover, this slight reaction is not confined to railroad circles alone. In other lines the same reaction occurs. The people's hopes and their eagerness have led them at first to overdo things; also on the appearance of the first new orders there springs up a fierce competition for a short time, which retards advancement and adversely affects prices.

Trunk lines show first benefit of increased earnings.—It is the decrease in expenses and the economies practised that have paved the way for increased earnings, not only for the railroads but in all other occupations as well. It is generally among the trunk lines, so called, that this gain is first noticeable. Formerly new railroad construction was one of the most important indications of improving times. This is not now so great a feature as in the past, the country having been pretty well gridironed by roads, but the expenditure for new rails and bridges to replace the old, and for new equipment, is greater than ever before.

Money from hiding places, new banks, etc.—As confidence grows money comes from its hiding places. Also, all kinds of products are now being grown and manufactured more freely. It is the function of banks to put both money and products into circulation, and there gradually spring up throughout the country many new banks to meet

these growing necessities. Each bank creates new currency and introduces new lines of credit in its vicinity, thus adding greatly to business activity. But there must be a demand for banks before they are organized; and the creation of products must precede the demand for their circulation by the bank.

The relatively low prices at this time of government bonds, which are used by the national banks as a basis for putting new notes into circulation, together with the increasing demand for money, make it profitable for old banks to take out additional circulation and for new ones to organize.

Public likes to buy on rising market.—We have seen that the rise in commodities begins early in pig iron, while the finished products are dull for a time thereafter; but when the change comes in the latter it is very rapid, and the advance in prices stimulates further purchasing. The public likes to buy on a rising market, as they think there is an opportunity to make money, while on a falling market they refrain from purchasing till the last moment, fearing a loss and desiring to buy as cheaply as possible.

Merchants increase orders.—When times improve merchants place larger orders and later on anticipate their wants, as successive rises in prices have taught them that there is money to be made in buying as largely as possible. At this time life insurance companies and savings banks increase their purchases of mortgages.

Slight cause may bring temporary reaction.—When the volume of business has increased and prices advance, in the very early stages of a prolonged rise, a comparatively slight cause may bring

about a temporary reaction—as too sudden a gain, any disturbing political or financial clouds on the horizon, etc. These are mere incidents in the upward tendency, birth pains, as it were, foreshadowing the greater prosperity to come.

Interest rates will go up enough to offset prices.—When commodity prices are rising, the interest rate will eventually advance an amount sufficient to offset the loss in the purchasing power of the principal, in order to retain the proper equilibrium. The plethora of money tempts people to borrow, thus creating a greater purchasing power; and these purchases increase the demand for money to produce and circulate them, thus raising interest rates.

Public now eager to buy on advance.—The rise in prices has now started in earnest, and the public, which required long continued rising values before becoming interested, is now becoming eager to purchase. It has been said "that a shortage of five per cent. in commodities or a rise in demand of that amount over supplies, starts competitive bidding that may raise prices as high as fifty per cent."

Consumption greater than production for a time.—In improving times consumption is greater than production for a while, so that in order to perceive the first proof of changing conditions one must scan closely the consumptive demands;* also outside conditions and happenings may have a great influence for the time being.

Improvements began some time before advance.—The surplus has to be worked off before any betterment in prices can take place. There must be plenty of orders on hand and a scarcity of material to fill them with. The betterment commences prob-

* Burton on Crises, p. 171.

ably six months before the rise in prices begins. Increasing prices, therefore, are not the first indication. The restoration of confidence awakens the people to their long neglected wants, and the rise in prices that follows indicates that conditions are reversing, and that consumption is outstripping supply.

Retailer cannot raise prices as fast as wholesaler.—When this rise in prices first occurs the retailer is at a disadvantage, as he cannot raise prices as fast as the wholesaler. He has to begin, as it were, a campaign of education along that line, and quietly accustom the public to paying an enhanced price.

Wages last to rise—Labor is the last to receive the benefit of rising prices in an enhanced wage, but shows it almost from the first in more hands employed and longer hours of work.

Laborers in raw materials get first raise—The first wages to be raised are the wages of those who are engaged in producing raw materials and manufacturing them. This rise is not important until competitive bidding sets in for the services of the workmen, and this cannot take place until idle labor is set to work, at least in those occupations where a rise is to occur.

Merchants, etc., can afford to pay higher interest.—As prices rise merchants and manufacturers can afford to pay higher rates of interest, because of the profits made by them out of the rising commodity prices.

A little income property bought.—Generally three or four years after a commercial panic there springs up a small demand for choice income property, the timid capitalist realizing that here is a solid investment that cannot "take unto itself wings

and fly away." This demand is small, being limited to a few wise investors, most of whom are not in business but who have money in the bank that must now be put to work to earn an income for the owner. Business property is on a firm basis, the inflation having by this time been squeezed out of it, but not yet out of vacant speculative holdings.

Speculation raises prices of grain so as to hurt exports.—At an early stage of the improvement speculation, that child of optimism, which is ever with us watching its opportunity, starts in, first in stocks and then in agricultural products, and raises prices, until, later on, prices for farm products become so high and our consumptive demand so great that our export business is seriously lessened. Our foreign customers at this period cannot afford to pay the enhanced prices, as conditions with them have not improved as much as with us. This for a while acts as a deterrent to better times, as it tends to prevent sales of these natural products and the beneficial effects of the circulation of the money their purchase price would yield; but conditions gradually improve abroad and prices for our farm products fall somewhat, so that at this time such conditions correct themselves without serious harm being done.

We import chiefly raw or partly manufactured materials.—Though our increasing orders for their wares materially help the foreigner from now on, these increased orders at first are mainly for goods only partly manufactured or for raw products that we can manufacture here.

Stages of progression.—We will here repeat the various stages of progress in mercantile circles that take place at this time. A working off of the sur-

plus through an increase in new orders is the first indication, and precedes a rise in prices. More workmen employed and at longer hours go before an advance in wages. Railroad repairs, betterments and, later, extensions or branches. Existing facilities for manufacture and for office quarters are gradually taxed to the utmost. This is followed by enlargement of these facilities, with the idea of reducing cost by producing more and at less expense, as through new machinery, improved business facilities, and the like.

IV.—Good Times

About Five Years After Commercial Panic.

[NOTE—*These conditions last occurred in* 1898. *If the next commercial panic takes place in* 1913, *for example, they may be expected substantially to repeat themselves about* 1918.]

ACTIVE rise in prices now.—When the steps previously explained have been taken and consumption still outstrips production, then comes an active rise in prices, instead of the cessation of price cutting, which was the earlier sign. New factories, new machinery, new office quarters and the like are created to meet the consumptive demand, which by this time is increasing faster than it can be provided for. Those things rise first which are most easily and speedily marketed.

Labor more fully employed than capital.—Labor is fully employed before capital is, so that now labor has the advantage, but ere long capital finds avenues in which to employ itself. Labor, having now the advantage of competitive bidding for its hire, experiences its first material rise and the country is prosperous.

Next wage rise in unskilled city laborers.—The rise in wages takes place now among the unskilled masses in the cities, those who do the preliminary work, as it were, connected with the necessaries of life. Later arises the demand for workers upon those articles that are more expensive, and finally upon luxuries.

Rise in wages helps raise prices.—The rise in wages acts as a stimulant to raise prices, not only by adding to the cost of production, but also by giving a greater purchasing power to the laboring classes.

Merchants enlarge their credit to buy goods.—Under the stimulus of rising prices the wholesaler and retailer, desirous of making all the profits they can through the continuing rise, order more and more goods, enlarging their credit for the purpose and so greatly increasing the demand for money.

Speculation grows on profits realized.—At first the use of money is confined mostly to strictly productive enterprise, but prospective profits have ever acted as a spur to speculation, so that the latter soon grows, modestly at first, but later to overshadow everything with its excesses.

Capital loses its timidity.—The field of operations must be attractive to induce capital, which is still timid, to enter, and these attractions must quietly increase and capital must realize its profits again and again before it finally loses its timidity, and becomes in the end overbold, overconfident, begetting a rashness of investment that in the future is to prove its undoing.

What increases in clearings indicate.—The first decided increase in bank clearings indicates stock speculation and some investing, and later an in-

creased volume of general business. Still further on the rise of commodity prices adds to the volume of clearings, as transactions in the same quantity of a commodity are represented by more money, owing to the higher price.

Benefits of crops felt mostly after opening of new year.—Good crops and fair prices, as we have seen, aid greatly toward better times, but as fall crops are not gathered until late in the season, we do not fully experience their beneficial effects until after the opening of the new year. They are then en route to market and the return flow of money in exchange for them slowly circulates through the various arteries of business life.

Cheerful tone to business.—The cheerful tone that now pervades all business is healthful and refreshing, a most gratifying change from the depression and ever deepening gloom of the last few years.

Interest depends on profits made.—Bankers and investors are now able to get satisfactory interest on their capital. The interest market, like the wage market, depends not so much on the volume of money in circulation as on the profits made. It is out of the fund of value created that both capital and labor must receive their shares, and the larger the fund the larger the return in both interest and wages. At this period the reservoir from which they both grow is steadily augmenting.

Confidence necessary for credit building.—Confidence is a basic necessity for all credit building; and the gradual growth of confidence is accompanied by a corresponding increase in credits, which helps the money market, gives a stimulus to business, and later, as we shall see, results in excesses which eventually bring about its own destruction.

What failures indicate.—One of the early signs of improvement was that total liabilities in failures were smaller but the number of failures larger, showing that failures were confined to the little fellows, while the concerns doing a larger business were at least holding their own. The next step is that failures become smaller both in number and in liabilities, showing that the strain under which they have been laboring for years past is now being removed from all classes.

Employers slow to employ new labor.—Employers at first hesitate to employ more hands or raise existing wages; when they do, it is an indication that the betterment has existed some little time. It is often when labor is complaining the most that a change for the better has set in. Labor, as wages begin to rise, gives very little trouble for a while, as the workman is continuously employed and often at an enhanced wage. He is fairly well satisfied, and prices have not yet risen enough to affect his buying capacity.

Western and Southern buyers first to give larger orders.—In drygoods the first sign of improvement is in the orders of Southern and Western buyers; but while the commodity rise commences in the West, it is overshadowed for some time to come in the bank clearings of the country as a whole by the increasing stock dealings of the East.

Test as to improvement.—The true test as to the extent of the business improvement comes after the first enthusiasm passes away. "At first there is a tendency to overbuy, due to a feeling of optimism (tinctured by speculation); the rebound, therefore, often goes too far, and now it is up to the purchasing capacity of the small consumer to help the deal-

ers out. This is the supreme test of business improvement, and is even more true in stocks."

Railroads accumulate a surplus.—At as early a period as possible some of the railroads adopt the policy of accumulating by adding to their surplus, in order to inspire confidence in their stock issues.

Imports of certain luxuries.—A further gain in imports indicates a continued growth in the purchasing power of the people. We are now not only importing for manufacturing purposes, as before, but the more necessary classes of luxuries as well are coming into demand.

How in early times we paid for imports.—At an early stage in our history, as with all new countries, we were debtors, and imports exceeded exports, the balance being made up by the sale abroad of interests in our resources. At first we sold our raw products and broad acres direct, but later sales were mostly in the shape of stocks and bonds, as that is the most convenient modern form of transferring ownership.

Later exported more than we imported.—As we gradually acquired the means to develop our resources we exported more than we imported, and this, because of our great natural wealth, brought money in ever increasing amounts to our shores.

Old nations have excess of imports.—As the resources of old nations are mostly developed, they, like a very young nation, import more than they export, and the balance is paid out of interest or principal owing to them from abroad, as in the case of England. They also sell to the newer country the products of their factories; for as each nation passes the earlier stages it goes more heavily into manufacturing, because of its abundant supply of labor.

How large supply of gold acts.—The increase in the supply of gold at first reduces interest rates, but as it gets into circulation it creates employment for itself, the demand that springs up is greater than the supply, and interest rates advance—especially as speculation, whose very life blood money is, starts in and gradually increases. The banker avails himself of the increasing supply of gold to make it the basis of credit. In the bank statement later on this credit appears as "deposits." The new gold affects first the prices of bonds and stocks, next the most necessary commodities, as wheat, cotton, corn, iron, steel and copper; later it affects all lines.

V.—Public Demand for Stocks

About Six Years after Commercial Panic.

[NOTE—*These conditions last occurred in* 1899. *If the next commercial panic takes place in* 1913, *for example, they may be expected substantially to repeat themselves about* 1919.]

DIFFERENCE between the public and investors.—A clean cut distinction should be drawn between the investing class and the public in general. Investors are attracted by low values, safety and good interest yield. The public go into stocks chiefly from speculative motives. With the public, value cuts but little figure. What they desire is a rapid rise in prices, and quick returns, often with little regard for intrinsic value. Rising prices long continued awaken their cupidity, and about this time they begin to make their appearance on 'change—veritable "lambs," as they are so aptly called.

Beginnings of Stock Exchange.—"It was on May 17, 1792, that twenty-four brokers met under a tree which grew on a spot opposite 60 Wall Street, and signed an agreement regarding a uniform rate of

commission, and afterward held irregular meetings at the Tontine Coffee House, Wall and Water Streets. This was the beginning of the Stock Exchange. In 1817 it was formally organized in the Merchants Exchange Building, now the Custom House. Ever since then New York has been the headquarters of the speculative tendencies of the country, with its great exchanges to facilitate the transfer of securities and commodities of all kinds.

Clearinghouse system adopted.—"It was not till 1890 that they adopted a clearing house system, when they awoke to the fact that instead of having to carry bank deposits to pay for stocks bought and sold, all that was necessary to carry was the balance between the two, and this was less than one-fortieth of the whole amount."*

Why bonds and stocks rise first.—As stocks and bonds are in a much more negotiable shape than an interest in a business enterprise not thus divided, and consequently are easier to buy and sell and more interesting to the speculator, they rise first and, naturally, sooner reach the limit of their rise, and are consequently the first to fall later on. Also, the public, being timid, prefer to invest in stocks and bonds because, in the main, these securities represent old and tried undertakings.

Stock rises always started by manipulators.—Stock rises have ever been started by manipulators, aided, of late years, by the purchases of a small class of investors who study values closely. The general public will not come in until after prices continue to rise for some time. This the professional understands and it is this inducement that he skilfully offers them from time to time. If his efforts are

* Securities as a Means of Payment, by C. A. Conant.

continued long enough he will be successful and the public will buy. quietly at first, but with a rush later on.

Public's surplus funds go into stocks.—At first stock investments are made from the surplus funds of the public and hence are by far the greatest at this time, after a long period of enforced saving. Business in general, while better, does not offer as yet sufficient inducement to idle capital; hence these surplus funds for some time past have been gradually seeking Wall Street. Stocks and bonds at this time pay a higher rate of interest than can be obtained in general business. Moreover, as business now requires a relatively small part of the funds seeking employment, New York banks are able to offer to their outside correspondents a rate of interest that causes a vast sum of money to accumulate in New York at the disposal of Wall Street; hence, later, the great rise that takes place and the many new companies formed. At no other time in the evolution of the cycle does Wall Street ever interest the public so greatly, or have such vast sums at its disposal.

Speculators want action.—Rapid fluctuations in market prices of stocks are attractive to the speculator, as he loves "action," and when values are advancing, having idle money, and having chafed through a long enforced repression of his energies, the inducements offered in this field prove vastly attractive to him.

Why stocks are so susceptible to influences.—Stocks fluctuate more than commodities and offer less resistance to surrounding influences, because their price depends on the rate of dividend they pay. This being the fact, they come into competition with

the market rates of interest, which change from day to day; and if these rates change in any great degree—because of a temporary stringency, a political happening, some important act of nature, etc.—the change is reflected almost at once in stocks.

Why commodities are slower to rise.—Commodities are, as a rule, slower in moving and so take longer time to be affected. Most events have passed by before they have time to change commodity prices to any important extent. The cause of the disturbance has to be great and to continue some time in order to affect commodities. The elements of labor, raw material, railroad rates and the like, all enter into commodity prices, in addition to interest on capital invested. An exception to this rule sometimes occurs in a time of general panic, when public fear may cause commodity prices to fall quickly.

Public often erroneously credited with good sense.—The public forget the losses of the past and go down to Wall Street as to a Mecca. They are too often credited with exercising good sense and learning from the losses of the past, when as a matter of fact, the cause may be either that their purchasing powers are impaired, or that interest returns on the investment are not sufficient, or that they can do better elsewhere.

Hopeful feeling runs into speculation.—On a rising market such as now exists in stocks, every one interested is hopeful and success breeds confidence; and if long continued this increasing hopeful feeling seeks expression in speculation, for it needs must have some outlet.

Lambs make money.—In the early part of this movement the lambs, perhaps for the only time in the financial cycle, have an opportunity to make

money in Wall Street. Their purchases are so large and so continuous and the volume of their savings is so great that they force stocks steadily up. The seasoned operator, after every fair rise, looks for a reaction and buys and sells accordingly; but there is no reaction to speak of for a long time because of the enormous sums pouring steadily into the market, so that his profits at this time often do not equal those of the lamb.

Europe sells us our stocks.—Europe, tempted by the higher prices and needing the money more than we do, is apt, on this advance, to sell us stocks in large amounts. But this has surprisingly little effect upon the market, so great is the investing and speculative movement and the purchasing power of the masses.

Shortage of stocks.—Later, to the surprise of all, the demand for securities exceeds the supply, enormous as it has seemed in the past. Stocks are steadily withdrawn from the market and blocks are taken up by financial heavyweights. The quiet growth of the country in wealth has overtaken the supply of securities, and promoters busy themselves and supply the demand on terms very liberal to themselves.

Good news sought for, bad unheeded.—On an improving market good items of news are eagerly sought for and made the most of, whereas bad news seems to fall on inattentive ears; and the reverse is true in periods of declining values.

Investing class increasing.—The investing class are constantly increasing, as our country matures, at the expense of the speculative element. As the country's wealth grows more substantial investors will ever exercise an increasing and beneficial influence on the stock and bond market, as they are

strongly opposed to speculative managements and dishonest methods and in favor of a conservative building up of values, with wise forethought for the dull days sure to come later on.

From the very nature of their methods they are bound to flourish and increase at the expense of the rash and often foolhardy speculative element. Speculators are far better suited to a new country, with its great natural resources, which require more or less chance-taking for development; but speculative methods stand little show of success (barring a very few exceptions) when opposed to the wiser methods of the true investor.

Ninety-five per cent. of business on credit.—Ninety-five per cent. of the business of the country is done on credit, and as Wall Street is the financial center of our country, it is there that the machinery of credit is regulated; hence the importance of Wall Street in business organization.

Credit system demands honesty in business.—This great increase in the use of credit instead of money will hereafter unceasingly demand a greater degree of honesty in business life. Credit must depend on confidence. The recent outbreak of indignation against the dishonest practices that have occurred in Wall Street for years past and heretofore have been only casually noticed, is in a measure an instance of this demand, and will continue until financial operations are conducted on a basis that will inspire confidence.

Credit expanding and more goods bought.—At this period in the cycle credit is expanding, and with the increasing volume of business and the advisability of carrying large stocks because of enhancing values, many abandon their former conservative

methods of doing business on a cash basis and taking advantage of the cash discount, which was more or less of a necessity in hard times if profits were to be made. They now make use of the credit offered them and buy more freely. This is one of the great factors in improving times; for money, as we have seen, can be very plentiful, yet the times be very hard.

Public, now possessed of credit, buys first bonds, then stocks.—Bank deposits, checks, bills of exchange, cable transfers, book accounts, bonds and notes are some of credit's efficient agents. Possessed of these, buyers investigate the opportunities offered to them for investment. As we have seen, they are invariably attracted first to the bond market; then, as bonds go up, and interest rates for money at the same time increase, they desert bonds for stocks, which not only pay a better rate of interest, but have the additional advantage of participating in the profits resulting from rising values. This introduces an element of speculation which bonds, with their fixed interest rates, lack.

Stocks, not bonds, get the increased profit.—The greater the amount of bonds outstanding against a corporation, the greater the percentage of profits coming to the stock as prosperity advances; for the bond, with its fixed interest rate, cannot participate in the increased earnings. The stock gets all the increase.

Demand for small currency.—A demand for small currency at this time indicates that the minor tradesmen and working classes are doing better, that they have money to keep in their tills and to carry about on their persons. This demand is ultimately so

great that it results in the government printing new issues of small denominations.

Circulation increases and raises prices.—The eager hunt for gold and silver during the hard times has resulted now in a large additional coinage. This, together with the increased circulation taken out by banks, adds greatly to the improving conditions and enhances prices. John Stuart Mill goes so far as to say on this subject that "If the whole money in circulation has doubled prices would be doubled. * * * A great increase in money is a certain harbinger of greater business, rising prices and increasing production." It is this great increase in the gold output that, later on, makes prices appear to be on a higher basis than they really are.

Low exchange rate indicates credit balance drawn on.—A low rate of exchange at this time, with steady gaining in percentage of imports over exports, indicates that our credit balance abroad is being drawn upon. As home consumption outruns production prices go up and, from then on, the increase in per cent. of shipments gradually favors imports as against exports.

Railroads increase both earnings and bond issues.—Railroads now not only show an increase in gross earnings, but a larger per cent. of gain in net, indicating better business combined with economy of management. There is peace between the various railroads now because there is a larger volume of traffic, sufficient for all, and therefore no occasion for fighting and rate cutting. The volume of borrowing is now greatly increased by railroads converting their short time notes into long time bonds, and adding new issues for necessary betterments and for their steadily increasing expenses.

Industrial companies gain more slowly.—Industrial companies do not reflect improving times as quickly as one would anticipate, because they have not only had old stocks to work off, in which there is but little profit, but they have orders to fill which were taken some time ago when times were dull and prices lower, which also yield but little profit.

Imports increase.—Having reached this degree of prosperity, we may export a moderate amount of gold, as we set a lower value on it than do those countries not so far advanced towards prosperous times. We have passed through the anxious stage, have ceased to hoard, and are disposed to purchase more goods abroad. Much of the merchandise thus imported is composed of materials for manufacturing purposes. Of course gold is the only kind of money we can settle our foreign obligations with, and moderate exports at this time are not to be viewed with alarm, as the return flow will soon set in.

Railroads now call for raw materials.—Money is now readily procurable in railroad circles through the sale of securities; and the urgent necessity of the roads for repairs and for additional rolling stock, owing to the increase in population that has been going on for years in contiguous territory, leads to a general railroad building and repairing movement. This causes a demand for labor and materials and for iron and coal, and hence a demand for iron and coal mines. Likewise, improving business creates a demand for new gold and silver mines, and new discoveries of copper mines follow the increasing use of copper in the building of electric roads, electric light and power companies, etc.

Money remains cheap.—Money, though now used in such vast quantities, at first remains cheap, to the

surprise of every one, the banker included. The constant percolation of money into the banks from many sources freshens the supply, and is the best indication of the quiet but great accretion of wealth, and the vast liquidation, that have quietly taken place during the hard times. Some of this money has perhaps been in hiding for years. Gold imports from abroad also increase our supply of cash.

Clearings reflect better times.—Improving times are reflected in the bank clearings of the day; a steady fall in cash and a rise in loans now indicate increasing business and enhancing values. Cash is now passing more rapidly from hand to hand in circulation, instead of remaining idle in the banks as formerly.

VI.—Era of Stock Speculation to Securities Panic

Six to Ten Years after Commercial Panic.

[NOTE.—*These conditions last occurred* 1899-1903. *If the next commercial panic takes place in* 1913, *for example, they may be expected to repeat themselves about* 1919-1923.]

COMMODITIES and equities rise in value.—As money increases in volume and circulation prices of commodities and of all securities possessing equities (as distinguished from bonds or mortgages covering only a fixed and invariable lien) tend to rise.

Rising prices make South and West active.—Rising prices and money in abundance start the West and South everywhere at work developing their natural resources. Improving times abroad are reflected in business circles here by an increasing demand for our products, modest at first but steadily growing.

Increasing speculation demands European gold.—Increasing volume of speculation creates a demand

for money. The golden tide is reversed, and commences to flow in steadily increasing volume to our shores from Europe under the stimulus of the higher interest paid here. Gold naturally seeks those countries where capital and industry are the best organized, where natural resources are the greatest, and where the greatest returns are coupled with a reasonable degree of safety of principal. These borrowings grow so extensive that they become the great factor in finally turning a credit into a debit balance against us abroad.

Easy security markets finance business undertakings.—This easy market for new and old securities alike facilitates greatly all business and railroad operations and finances our great undertakings. There is a marked and natural tendency at this period of the cycle toward financial concentration to meet the requirements of the times. As the country grows and business organization develops, larger and larger sums of money are required to finance important enterprises. Large organizations are more desirable, effective and economical than smaller ones, as great savings can be effected in purchases of raw material, in manufacturing, and in placing goods on the market, where capital and volume of business are large.

The people's money makes the financier.—It is for the most part the money of the people accumulated in banks and trust companies that supplies the funds to negotiate these great undertakings, and not the money of any rich individual or coterie of capitalists. On the contrary, it is the use of the people's money that has created the multimillionaire, and without this fund to draw from he would never have existed.

Great gold output helps keep up agricultural prices.—The great output of gold and increased issues of other currency during this period help make better times by raising prices. This is especially important as affecting the prices of agricultural products, which always form the most essential foundation for real prosperity.

This is best time for majority.—The best period for the majority of our people, and the healthiest financially, is now, before stock prices have gone too high, and before the period of excessive speculation and extravagance has begun. Debts have been paid and all are remuneratively employed. Frugality, temperance and the greatest amount of honesty we experience in business life, govern our actions. Commodities and wages have risen sufficiently to be remunerative, but are not excessive. At this time almost everyone in business can save money, if he is so disposed, and is not mentally or physically disqualified.

There is a gradual decrease in the amount of mortgages foreclosed, and also, for a time (until the realty market gets active later on) of new mortgages given.

Great movements begin with great bank reserves.—Great movements in business or speculation have their commencement in large bank reserves, and end when the surplus of reserves over reserve requirements has been brought down to a minimum. These surplus reserves diminish when good times are in full operation, and increase as the times grow poorer and less money is employed in business and speculation.

Savings banks and trust companies have money to loan.—The savings banks and trust companies, "the

one the depository of the provident poor, the other of the provident rich," have both grown in importance and have large amounts of money to invest—the former in safe investments regulated by law, while the latter too often at this time place large sums at the disposal of powerful manipulators for stock promotion or stock jobbing purposes.

Price fluctuations not so injurious when market is scantily supplied.—Fluctuation in the price of commodities is not nearly as injurious now in its effects, when the market is scantily supplied, as when it has an overabundance of commodities on hand; and failures are far less frequent in the former than in the latter case.

Advancing commodity prices.—One of the best indications of the consuming power of the people is commodity prices; when these are advancing an improving condition of the public purse is indicated, and when the advance is very rapid the presence of more or less speculation is shown.

Stock market generally barometer of uninvested capital.—The stock market is the barometer of the supply of uninvested capital and the demand for it; with the exception, however, of those times when fear has taken possession of the market, or when stocks are temporarily a discredited investment. Stocks are preferred to real estate by investors and speculators because of the much quicker action in buying and selling, and because the cost of transfer and the trouble connected therewith are so much less, only a few hours being required, as against a much longer time for the selection and transfer of real estate; nor are there bad titles to cause long delays or endless litigation. If listed on Wall

Street, especially, stocks have that most important feature in estimating value—easy convertibility.

Stocks susceptible to money market.—It takes cash to buy stocks, so stocks are very susceptible to any influence, either passing or permanent, that affects the supply of ready money; hence the frequent smaller panics on Wall Street that have but little influence on the country at large.

Stock buying a popular craze.—Stock purchasing now becomes a popular craze, and the printing presses are kept busy morning, noon and night, striking off handsomely lithographed stocks, many of doubtful worth, which are sold to the unsophisticated at prices often far above their real value.

Tricks of manipulators.—The unscrupulous manipulator circulates stories of many kinds, all calculated to work on the imagination of the lamb and induce him to buy, and constantly manipulates prices so far as he is able, with the purpose of transferring money from the pockets of the innocents to his own. He makes fictitious purchases and sales to offset each other, but which will appear in the public prints as purchases or sales, and thus convey the idea to his victim that there is great activity in the particular stock or stocks that he is for the time being offering. Even securities of easy virtue attract now, and the desire to get rich quick grows among the people, as it always will if prosperity lasts long enough.

Speculation runs riot.—At this time, when the unused funds of the United States and Europe are at the disposal of Wall Street, it is natural that speculation runs riot, and there comes a period of excess that might well be called the "merger and promotion period," because of the great activity of pro-

moters. It is only after a long period of false hopes and promises temptingly held forth, that the foolish public finally ask the professional to make good; and when he fails to do so, the public become discouraged and sell, and condemn good and bad alike.

Supply of money becomes exhausted, and public become disgusted.—As it is easier to create new companies than it is new money, the supply of the latter becomes finally exhausted, and credit as well. The public gradually withdraw their confidence and purchase fewer stocks, and as prices shrink their eyes are opened (for few speculators can see the error of their ways as long as they are successful). Disgust gradually takes the place of their old time enthusiasm, and money is withdrawn steadily from Wall Street. But before this has taken place the manipulator, desirous of exchanging his paper profits for hard cash, has unloaded vast amounts of stocks upon the shoulders of unwary lambs.

When bad news does not affect prices.—When bad news does not affect stock values adversely but prices rise instead, it is an indication that stocks are under the control of cliques, and that they are raising prices for their own purposes.

Prior to securities panic, a decline in stock values.—For two or three years before a securities panic there is a gradual decline in stocks, but this does not affect commodity values to any great extent, as money is still depreciating, owing to the larger gold output and the inflation of currency, and growing confidence is increasing its circulation. The general want of confidence that sets in is directed solely against Wall Street and corporate mismanagement there. Money is withdrawn gradually from stocks,

but there is plenty to be had at normal rates for general business purposes.

Merchants now in safe condition.—The merchants are in a healthy financial condition, very conservative, owing but little, with prices as yet reasonable, and therefore in no condition to be severely injured by a panic. The few among them who do fail later on, have either lost heavily in stock speculation, or belong to that class who venture everything on small margins, so that the continuance of good times alone can keep them afloat, or are otherwise in a bad way for some special reason.

Great rise or fall preceded by long dull spell.—Any great rise or decline in stocks is generally preceded by a long continued dull season. If they have unduly risen it precedes a fall, if they are excessively depressed it goes before the rise—which, however, may be a long time in coming.

Long decline shakes out weak holders.—When stocks have been going down for some time weak holders are shaken out. A short interest is built up and stocks go into strong hands.

Long rise develops weakness in holders.—On the contrary, during a long continued rise stocks pass from strong hands into weak ones, pyramiding takes place and overexpansion of credit develops. This weakens the market and renders it liable to suffer from vigorous attacks of the bears. The market strengthens as stocks decline and weakens as they advance, thus carrying within itself the natural remedy for an excess in either direction.

Securities market discounts coming events.—The securities market, in its advances and declines, discounts coming events, and is more easily affected by psychological reasons than is the merchant or the

manufacturer. This is chiefly because the money market acts quicker and more thoroughly on Wall Street securities, which are more mobile, than it does on commodities, as before explained.

Public has financial gastritis.—With the speculative public disgusted and their stock purchasing power at an end, with prices topheavy and stocks thoroughly watered, financial gastritis sets in, brought about by trying to absorb too many indigestible securities.

Minor panic may occur two or three years before greater one.—Under the great strain put upon the money market the weakest point has to give way, and that is an inflated stock market. A selling movement starts in and a minor panic may take place on 'change about two or three years before the genuine securities panic arrives. The people sell and continue to sell thereafter, and prices steadily fall.

Professionals unable to support market.—Manipulators and professionals at this time buy to protect their other holdings, and a little later because they think stocks are a good purchase; but finally the volume of sales is so great and continuous and prices fall so abominably, that the professional eventually reaches the limit of his capacity to buy, having exhausted his credit here and abroad. With insufficient buyers and liberal offers of stock at falling prices, and a stringent money market in Wall Street, the crash finally takes place and the Financial Panic is on.

Résumé of events.—A brief résumé of the happenings is as follows: Speculators start the buying, bankers encourage it, the public later begins to get excited at the sight of sudden wealth easily acquired

and buys right and left at high prices. Speculators thereupon nurse and stimulate the excitement by reports of what is to happen next; prices rise to a point where they can go no higher, and the public becomes impatient and frightened. The banks' resources are exhausted, and excessively high money rates coincide with unmistakable signs that insiders are selling out to the public and realizing their paper profits. With stock prices so high as to yield but scant interest, and with no more money in sight to draw upon for purposes of stock speculation, overstrained confidence is shattered, and everyone tries to sell and no one to buy. Rotten disclosures are now due to come to the surface and the crash follows.

VII.—After Securities Panic to Excessive Prosperity

About 10 to 12 Years after Commercial Panic.

[NOTE—*These conditions last occurred* 1903-1905. *If the next commercial panic takes place in* 1913, *for example, they may be expected to repeat themselves about* 1923-1925.]

FEW business men foresee the panic.—Comparatively few have foreseen the panic, as business conditions remain so good and business men in general are so immersed in their own affairs that they do not watch the operations of the Stock Exchange closely; nor do they bother with what apparently does not concern them.

Panic affects speculators worst, and business only to a small extent.—It is confined in a great degree to the speculative element, and to banks doing a Wall Street business. The business interests of the country at this time occupy the position of creditor and owe little or nothing; whereas Wall Street, being the home of stocks and bonds, is a heavy debtor, owing every source it can borrow from at home and abroad, and never ceasing to borrow until its credit is exhausted and the crash comes,

when payment is demanded. For this reason the effects of the panic are mostly confined to Wall Street, and while affecting business for a year thereafter through the money market, most of the effect is of a sympathetic nature and affects the sale of luxuries more than anything else. The panic is a rich man's affair, the public having mostly sold out to the rich speculator, as we have seen. The cause is not serious enough to affect labor to any marked degree, and consequently has but small influence on the prices of the necessaries of life.

Panic makes labor reasonable.—It, however, has one very beneficial effect on labor. Labor has been so fully employed, and at so much higher wages, that its demands (as in 1902) have become very unreasonable; continued success and compliance with its wishes have, as is usual with human nature, been too much for it, and the lesson administered after a security panic brings its demands back to a more reasonable basis.

A credit panic.—The Securities or Financial Panic is a credit crisis and is not accompanied outside of Wall Street by money stringency due to exhaustion of credit and over-action of money in all lines and conversion of liquid capital into fixed value, as is the case in a commercial panic. This is shown by the low rate of interest paid by merchants, even during the panic.

Securities and commercial panic compared.—The securities panic is the result of overproduction and speculation in stocks and stocks only, whereas the commercial panic is preceded by an inflation of stock prices and of all industrial and commercial values and by great indebtedness, and followed by a great fall in prices of commodities and real estate, as well

as of stocks. Both panics are preceded by extravagance and the prices reached and indebtedness incurred strain credit; but in the former case credit is withdrawn from stocks only, in the latter a withdrawal of money and credit from stocks, business and speculation occurs.

When iron and steel fall.—Iron and steel prices, generally recognized as a barometer of trade, behave differently in the two kinds of panics. When a securities panic is impending they do not fall until just before or just after the panic, as this panic is confined mainly to securities and business lines are but slightly affected. In a general commercial panic, on the other hand, iron and steel begin to fall at an early stage of the decline in general prices.

Money leaves Wall Street and goes into business.—The money of the country is now diverted from Wall Street speculation and placed once more in general lines in which the owner has confidence. The public have lost faith in Wall Street, have demanded an accounting, and are transferring their business elsewhere, thoroughly displeased with stock speculation. This transferrence is indicated at the time by increasing loans in business lines, while great liquidation is going on in stocks. After the panic, however, there is a disinclination for a time to undertake new operations which will tie up capital and change it into fixed values, until the capitalist can quietly investigate the situation and become positive as to how far the damage will extend, but this is only a short halt.

Losses to banks not near as heavy as after commercial panic.—The Wall Street obligations do not entail nearly as heavy losses on banks as do the heavy borrowings of all classes prior to a commer-

cial panic; for the former are, of late years, generally well secured on stock collateral, and the banker has learned from experience to sell out this collateral in time to secure himself.

West suffers less than East.—The West being the home of the natural product and having indulged in very little stock speculation, suffers much less than the East, especially New York City, which is the center of stock transactions. The damage to the West is mainly in the temporary slowing up of business during the continuance of fear and the liquidation that results; but the East, being the financial center, is most affected by a panic that is mainly financial.

Rich mostly affected.—The few failures, the comparatively quick improvement in stock prices, the fact that business is so little injured and that earnings of railroads during and after a securities panic are but little affected, show that the wealthy bear most of the losses. There were no intrinsic defects in most of the securities which suffered, but excessive stock speculation, inflating values wildly and tying up a large amount of liquid capital needed in other lines, resulted in temporary congestion of the money market.

Recovery quick.—The recovery is far quicker than after a commercial panic, a year being about the extent of it, for stocks are in themselves semi-liquid and therefore the liquidation is much easier effected than when it has to permeate all lines of business, ending up in real estate.

Outside of Wall Street people have been saving money.—While many have speculated, yet the percentage is comparatively small when spread all through the country. Many of the public deserted

the market at an early date, when it lost the attraction of constantly increasing values. Most people have beeen employed and have saved money, and the railroads and farmers are doing well. Wall Street is the one spot financially diseased.

Public slow to return to Wall Street.—When the public desert stocks and go into other lines of investment or business, as they do after a securities panic, it is a long time before they wander back, and in the meantime prices have to react. The public must believe that the investment is a tempting one before they return—not that they ever purchase in large amounts at the lowest figures, for they do not; rising prices and the hope of their going up still further are always the temptation that induces renewed speculative buying. It is only the regular investors who are wise enough to recognize bargains and buy them.

Bank customers have to pay up for stocks.—For months after the securities panic bank clients have to redeem from the banks inferior securities given as collateral, that the public would not take, and are obliged to sacrifice good ones to do so. In 1903, in order to do this immense borrowings and credits had to be obtained abroad, and these extended to a point that led to just criticism of our credits and methods.

European crops.—At the time of our financial panic if Europe has had poor crops the effects of the panic are apt to be more severe, as it closes much of that market to our bargain sales. We cannot under these circumstances sell Europe both crops and stocks, and as a result the latter have to suffer.

Some effects of securities panic.—The securities

crisis cuts down profits and reduces the volume of business, and for a very short time a few hands are discharged from shops and factories. It is, however, the sale of pictures, the receipts of swell restaurants, etc., that feel its worst effects, and most of this in New York City. Wall Street and Fifth Avenue suffer most.

Origin of losses.—Much of the loss that is sustained in a securities panic comes from downright rascality in formation of some new companies and watering of the old, the misleading information put forth, and the excessive booming of stocks through rank manipulation. The remainder the public must lay to the gambling spirit that possesses them.

Shrinkage in bank clearings.—It is well to remember that the shrinkage in bank clearings is mostly confined to the East, especially New York City, and that the loss, if analyzed, is in a measure due to the elimination of past speculative purchases, and sales of stocks at lower figures. However, quite a percentage of previous sales of stocks at higher prices have been on "matched orders," and the letting of the wind out of these bubbles is really a benefit to the community. Commodity sales are larger than thought, as prices are still low, so that such sales do not show up in the volume of clearings for as much as they are really entitled to. The quiet improvement that sets in later on in business circles is not noticed as soon as it should be, owing to the fact that it is overshadowed in the East by the great shrinkage in stock sales.

European loans after panic.—After the panic, for as long a period as fear is a prominent feature, few great railroad or other loans can be negotiated here and applications of this nature have to be taken to

Europe, and unless they are very good and the price reduced considerably so as to tempt buyers, they will not be accepted. In Europe there is a large investing class who have money and are not involved to any great extent and these become purchasers.

Incorporations.—As the times improve in business lines there are numerous incorporations, mostly at first for manufacturing purposes that supply the increasing demand for commodities, next for building and real estate purposes in the large cities, and later on for speculation in these lines.

Mostly speculators who get benefit of stock rise.—The public are now so interested in other affairs and their experience with stocks has been so recent and disastrous, that they have not again acquired a fancy for stock speculation; so that when times improve sufficiently to warrant an advance in stocks, it is mostly the professional and investing class who reap the harvest, and not so much the speculative public in general as was the case before. Professionals, as usual, borrow money in every direction, and Europe and the West contribute largely, attracted by the high rates of interest that finally prevail on Wall Street.

Staple investments.—Many of the public are now in favor of more staple investments than stocks, something that the purchaser can control himself, so they invest their money in factories, warehouses, home building, realty and business, and much of this capital ceases to be circulating.

Mining stock craze on.—Others are smitten with a craze (for such it eventually amounts to) to invest in mining stocks, which spring up as it were from under a magician's wand to tap the hidden

sources of wealth. The tools used often seem to be the printing press, the post offce, and a few acres of land thrown in—rock, if possible, and preferably inaccessible or near some good mine, providing it can be bought for a song. Often a hole scooped out of the ground a few feet deep, is all that is necessary, so that the owners can expatiate learnedly about "development work," for the purchaser never cares to inspect it. It is also well to be a little lavish in issuing a fine stock certificate, one that will appeal to the purchaser's imagination, and with a fluent talker at the office one is ready for business. This movement, like others of its kind, originally started with solid merit as a foundation. Those whose business it is have for some time past been hard at work developing mines and putting them on a paying basis.

In boom times ordinary rules of common sense do not govern.—We must remember that in boom tims a psychological influence is exerted, exercising as it were an intoxicating effect, the natural outgrowth of long continued success, and that at this time the ordinary standards of common sense do not govern and dreams appear to many as actualities.

Clerks and artisans have saved money.—All through the hard times there has been a large class of clerks and artisans who, having had steady work at fair wages, have been able because of the low prices to save up money. Many of them have lived in cramped quarters and disagreeable neighborhoods, and long for a detached home, with fresh air and better social surroundings, to bring up a family in. Rents have risen as vacant houses grow scarcer, and competition sets in, until finally it is cheaper to build, because of the reasonable price of

lots and building materials, than it is to pay rent. It is this class, and not the rich, that now start a building movement—at first mostly towards the outskirts, where they can better afford to live.

When houses pay.—As a well-known writer says, "If the rents of houses pay better than money at interest, houses will advance rapidly in selling value, and the owner of capital at interest will call it in, hire men, buy material and build houses, until the old equilibrium between capital in houses and capital at interest is restored."

Investment movement in realty.—For a long time (three to five years) this is an investment movement only. The buying of vacant tracts for subdivision, and by the builder who intends to build thereon, is at this period entirely legitimate, as they are intended to supply a want—not merely to pass from hand to hand at higher and higher prices in a continuous gamble. The proof that the movement is not at first speculative is disclosed by the fact that lots not needed for building purposes are neglected and as unsalable as ever, while those that have this value attached to them gradually rise in price. This rise is normal, and finally makes a good many friendly toward real estate who have hitherto preferred stocks. This realty movement may start in about a year before the securities panic in those cities that have received the greatest increase in population, like New York City, Seattle or Los Angeles in recent years. In other cities it does not start until nearly a year after the panic.

VIII.—Excessive Prosperity to Waning of Stock Boom

About 12 to 13 Years after Commercial Panic.

[NOTE—*These conditions last occurred* 1905-1906. *If the next commercial panic takes place in* 1913, *for example, they may be expected to repeat themselves about* 1925-1926.]

MONEY and confidence beget rise in prices. —The history of economics has always shown that an abundance of cheap money and long time credits, with confidence (the presence of which is now shown by the feverish pace of enterprise) and rising prices, especially if augmented by a great increase in gold output, sooner or later develop inflation and speculation. People are tempted to go heavily in debt. The use of this credit increases the demand for commodities, causing them to circulate rapidly by reason of their ready sale. That is necessary before they can boom. All this enhances prices and results in a greater demand for money and a consequent rise in interest rates. This movement spreads through all forms of fixed capital, and when sufficiently inter-

esting is taken up by the speculator and continued to exhaustion.

Many new companies organized.—Company promotion booms follow the tide of prosperity. The great amount of money and credit in circulation begets the desire to utilize them. The best and quickest way to do so is through company organization.

A period of excess.—We are now entering upon an era of excessive development, internal improvements and railroad building, of overproduction and overaction in all lines, commencing with stocks and ending up in real estate—a period when prices are raised to an extreme so great that the public finally becomes rebellious.

Many not now interested in stocks.—Only a part of the speculative public is interested in stocks after the financial panic. The main enhancement in prices at that time is the work of the rich cliques and manipulators, supported by a steady investment buying. This is shown by the fact that after the great fall in the stock market when business gets the upper hand (as in March, 1907) there are comparatively few failures in the business world. That the manipulators and capitalists interested in the stock market are rich, is shown by their ability to put up additional collateral on a rapidly falling market, and eventually to stand the very severe losses entailed by the crash, without failing themselves and bringing down others with them.

Choice bonds languish.—Choice bonds, with their small fixed interest rates, begin to languish, and more doubtful issues yielding a larger income are for a time in favor; but a further rise in interest rates finally makes even these second

class bonds unsalable. This tendency of bonds to fall indicates that interest rates are advancing and are now too high to allow bonds to compete, hence bonds fall in price in a further endeavor to hold their place in the money market. This drives many investors into speculative stock issues or other investments that are perhaps not conservative or even safe. It also indicates that both increasing business and speculation are making greater demands on the money market.

Commodity prices rise.—Commodity prices also rise with interest rates, and so increase the demand for money and credit. The greatest rise in commodity prices in boom times is in primary commodities—those needed by manufacturers. These increases in prices stimulate mercantile classes to greater activity and larger purchases, and the banks are spurred on to increase their lines of credit.

Money begins to go from stocks into business.—As their business grows, many business men withdraw their capital from Wall Street and devote their time and money to their own enterprises; and the first serious setback to the rapid rise in prices causes many to desert the Street and leave the field thereafter to the manipulator and simon-pure investor.

Investors become speculators.—When stocks yield but small returns on the selling price and interest rates are high, the main inducement to buy stocks is the hope of a rise. The buyer now becomes a speculator, not an investor.

Your genuine investor, if wise (but many hold on) then sells his stocks, places his money elsewhere, and leaves the market to the professionals and cliques to fight it out as they see fit. Battles royal often take place between these great warring inter-

ests, in which the small speculator may be gathered up incidentally by either party and landed on some side street, as it were, shorn of his cash and possibly conscious of the foolish part he has been acting.

Stock market passes to a speculative basis.—The stock market has now passed from an investment to a speculative basis, as is evidenced by the fact that dividend yields on stocks are considerably below commercial rates of interest. At this time rumors are much used to enhance or maintain prices, and this helps to mark the change.

We become world's creditors.—In February, 1905, we ceased temporarily to feed the world with food, but gave it gold instead, paying up our foreign debts and loaning foreigners, for the first time, part of our surplus gold. We thus made our initial entry into the list of creditor nations. We are not a very important factor in the list as yet, but are likely to increase greatly in the future along these lines. Our wealth is rapidly increasing because, owing to machinery and better methods, one man's work now produces several times as much as it did in 1850, and from what was formerly wasted, fortunes are being made.

High rate of exchange.—A high or rising rate of exchange at this time often indicates an increase of indebtedness, or it may mean that our exports are light.

What continued prosperity brings.—Long continued prosperity brings inflation of prices and credit and consolidation of great interests, unprecedented construction, high priced labor and generous living. Extravagance is greatly increased by easy credit and successful speculation. When the people

have money it is human nature to spend it and even to run into debt.

Failures decrease.—At these times, when prices are rapidly augmenting and sales are easy, there are fewer failures, for the debtor can quickly dispose of his properties at constantly increasing prices, and this, together with the ease with which credits can be obtained, permits him to pay up and acquire new indebtedness—to swap it, as it were, and so keep his credit good for the time being.

Sales of our bonds and stocks in Europe diminish.—Also improved times in Europe now raise interest rates there and so lessen the foreign demand for our stocks and bonds; especially the latter, because of their small interest and their non-participating character.

New gold fields.—The large amount of money and credit now available, together with improved labor-saving devices and new chemical and engineering methods, make it easy to get money to explore new gold and copper fields, and the great amount of gold obtained adds to prices and speculation.

The effect of this increased gold output is more noticeable in those countries where the credit system is well developed by means of banks, than it is in other countries where exchanges of commodities are chiefly effected by the circulation of money from hand to hand; as the banker uses the new gold as a basis of credit expansion, forming a sort of additional credit circulation. Increased rapidity of circulation has the effect, as we have seen, of a greater supply.

Public think prosperity will last.—At this period, when most events are favorable, the impression permeates the masses that these conditions are to con-

tinue indefinitely, that supplies are short and the demand great, and this acts as a stimulus to advance prices still further.

Realty becomes a competitor with savings banks.—Real estate operations are now making large demands on the money market, and become a competitor with the savings banks for the earnings of the people. This affects bank balances greatly for several years.

People demand better transit.—Now springs up a demand for better transit facilities in the overcrowded cities, due not only to the increase in population, but to the sale of lots in the outskirts to the poorer classes for homes. People living in these districts, as their numbers increase, demand better transit facilities to and from their business. Later on this real estate movement broadens out into speculation, and the demand then becomes more insistent than ever.

Famine of small currency indicates more active trade.—A currency famine setting in with a scarcity of small bills is a sure sign of active trade, indicating as it does that people are carrying more money about their persons and consequently spending more, and that the small trader is keeping more on hand in his till for business purposes.

Increase in circulation begets excessive loans.—A steady and large increase in circulation makes it easier for the banks to grant excessive loans and discounts, and so overstimulates business. The very ease with which debts can be incurred in good times proves often an irresistible inducement to many to assume obligations which later on they cannot meet.

When business is good merchants do not worry.—When merchants have more than they can attend

to (as in 1906) they are so pre-occupied in business lines that there is a disposition to let the future take care of itself when any disturbing features arise, and to trust to the good sense of the people; so they do not worry as much as they do in poorer times over threatened legislation or the disastrous losses arising from great fires, earthquakes and the like.

Modern business puts small concerns at a disadvantage.—Our modern methods of doing business on as small a margin of profit as possible, and the great cost of modern machinery, have made it necessary, in many lines, to have a very large capital at one's disposal in order to do business on the most economical basis. This places individual firms at a great disadvantage, and they have to give way to large corporations with greater capital and influence. Individual ownership and old business methods are fast becoming a thing of the past, and this tendency will continue to grow as the supply of capital increases. As one writer aptly puts it, "economic evolution is making for the triumph of the strong combination over the weak individual."

Corporate management as honest as private.—Notwithstanding all that has been said to the contrary, we shall probably find as much honesty under corporate management as under private control, and in time the former, being more subject to public inspection and legislative action, will become the favorite of the two, especially as corporations are less likely to fail; but perhaps it will have to be eventually on a cooperative basis, where all employees participate in the profits.

Commercial banks should not pay interest.—The bad habit of banks (other than savings) offering interest, compels the banks to seek a high rate of in-

terest in order to recoup themselves for the interest they are paying. Oftentimes the rate the bank must earn is so high that only the speculative mind can see any profit (real or imagined) in borrowing at such rates. This attracts an undesirable class of loans, and so sows the seeds of future trouble for the bank. Also, such banks are not safeguarded by the same laws as savings banks, and hence are not as safe a depository.

Small reactions good.—From time to time in the upward movement small reactions occur. These are remedial and corrective and indicate that the upward swing is becoming too rapid and dangerous and that a slowing down is temporarily advisable.

Speculation active.—Fascinated by the rapid rise in prices, as one writer says, many now join in the speculative movement and ride gaily to a cropper, and bankers and brokers are too often found encouraging a speculation that brings them business. Easy credit and plenty of money are ever great factors in creating speculation. Many companies have at this time such a large amount of surplus profits that it becomes fairly burdensome, and it is natural that these funds should be easily diverted to speculation. The professional manipulator encourages and stimulates the excitement by reports of what is to happen next, and plays upon the hopes or fears of the public as a musician would on an instrument. An intense ambition to acquire money now leads frequently to an abuse of credit.

Most attractive ventures taken up first.—The speculator selects the ventures which are most attractive, promising the greatest returns, and these are taken up in the regular order of their financial attractiveness, real estate being last.

It is action that your true speculator desires, a chance to guess, and hope and conceit delude him with the idea that he will come out a winner. As Thomas Gibson says, "Speculation in moderation, connected with natural fluctuation in values based on the law of supply and demand, is wholesome and legitimate, but is bad if connected with artificial fluctuations; the latter is simply a gambling employment of capital, bad for legitimate business and for those engaged in speculation as well. This fictitious species of speculation, bearing within itself no means of improving, on the average, the means of those engaged in it, must clearly result, in the long run, unsatisfactorily to the speculator. It is a guess at what is going to be. The fascination of hope keeps the speculator in the field till his last dollar is spent. In this way speculation fixes its own limits and naturally wears itself out."

Mr. Gibson, in "Pitfalls of Speculation," taking 4,000 speculative accounts in stocks and cereals, extending over a period of ten years, finds that 80 per cent. showed a final loss, that the tendency to buy at the top and sell at the bottom was most prevalent, and that most of the operations appeared to be of a purely gambling nature. The further fact was established that they universally led to excesses. He says: "Speculation feeds upon wide and frequent fluctuations and wanes as values become steadier, whereas unsteadiness interferes with the employment of capital in legitimate business."

One line may absorb too much money.—At this time and thereafter, one source of investment, as stocks, real estate, etc., may absorb an undue amount of money, thereby not only crippling other lines for awhile because cash and credit are with-

held from them, but even becoming dangerous as a result of excessive capital being drawn into the one channel.

City attracts country men.—The movement toward the cities that now takes places is in search of the greatest opportunities and attractions. The cities offer superior opportunities to labor, greater social advantages, and wider range of entertainment. Their attractive power is therefore very great, and ultimately a surplus of labor in the great cities results. Later, when times become stringent, the tide of population ebbs back to the country again. The subtraction of population from the country, while in many ways a great inconvenience, yet benefits the farmer, as it adds to consumers and subtracts from agricultural producers, and so tends to raise the prices of farm products.

Increasing use of machinery.—The quantity of food and raw materials consumable by each human being is limited, whereas the value that machinery may add to materials, is almost or quite illimitable. One dollar's worth of material is often manufactured into many hundreds of dollars' worth of products. Thus the proportion of machinery to population is continually increasing and that of itself, under ordinary circumstances, must cause a moderate, natural and continued flow of population from agriculture to manufactures, from country to city life. Improved machinery makes the trades at least temporarily more remunerative than farming; but this is being constantly offset by the application of better machinery and methods to agriculture, making it more profitable and pleasant.

No ordinary event can check great economic laws.—The economic laws which determine production,

distribution and consumption, are too great to be stopped in their onward progress by even extraordinary happenings. Thus the great fire in New York in 1835, with all its enormous destruction of capital, did not stop the real estate boom then on, nor did the Spanish war, the Russo-Japanese conflict, or the great 'Frisco fire in 1906, stop the good times; showing how great is the impetus when one of these movements gets fully under way. It moves on as irresistibly as destiny itself, unless at the time of these events the apex of prosperity has been nearly reached, so that the workings of the law favor or would soon favor a decline.

The influence of such happenings is at the moment merely to accelerate or retard the workings of the law, not to upset its action. The great burden of the losses inflicted is felt later, when the decline is reached.

Manufacturer forced to produce cheaper.—The rise in wages and materials, by reducing the profits of the manufacturer, forces him to adopt means that will reduce the cost of production and distribution, such as improved machinery, better factories and better business methods. These often work a hardship for the individual later on, as he may have overenlarged his plant or overextended his operations; but the public sooner or later gets the benefit in reduced prices.

Money still coming from West and Europe.—Money, attracted by the high rates in New York, comes here from the West and from Europe still, and is principally occupied on Wall Street in maintaining the high prices now prevalent there.

Real estate.—Real estate, being the most permanent form of investment, is the last developed and

the last in which speculation sets in; it has begun, as we have seen, in an investment movement, shortly after the securities panic and in certain cities even before; but, proving profitable, it now attracts (in cities receiving the greatest tide of immigration and advertising) the attention of the speculator. As real estate goes up in price, it tends to increase the cost of production, as rent enters largely into the cost of living, factory and office sites, railroad terminals, etc. The extension of main and branch line railroads necessitates new towns, and these are now seized upon by the speculator as presenting a good opportunity to realize quick profits.

Employers concede to striking workmen.—The working man is now well employed and does not so often indulge in strikes, and when he does they are sooner settled. Employers generally concede the most, as they cannot afford to risk a shut-down when orders may already be behindhand. Strikes are consequently not, as a rule, so bitter, unless the recognition of the trade union is required, in which case they are more lasting and harder to handle.

Rise in wages.—There comes a larger and more substantial rise in wages when prosperity has sufficiently progressed, and prices have advanced enough to warrant corporations paying larger or additional dividends. The great scarcity of men, and the very important fact that business is so good, makes employers yield in whole or in part to the demands of their employees. The worker argues that everything costs him more and it is only fair he should have some benefit from the better times. The rise in wages, however, is very seldom commensurate with the rise in commodity prices, so that if it were not for the more steady employment and longer hours

in certain lines and the larger number employed, it would work a universal hardship on the workmen. In fact, it does in many cases, and those suffer who are living on a fixed income and have to meet increased expenses. To this class the high prices may seem almost unbearable before the reaction comes.

Trade unions grow.—Good times encourage the growth and extension of trade unions, begetting a spirit of independence in the men and a disposition often to throw up an occupation which may not be to their entire satisfaction.

Immigration grows.—Immigration is greater as prosperity increases and becomes known abroad and advertised, as it were, by the remittances that foreigners here send to their friends in Europe. Some of these remittances are used to purchase tickets for our shores. The news of the arrival of the money spreads rapidly where it is received and the advice to come here induces many to start and try their luck, hoping to do as well as the sender, whom they generally know.

Railroads buy other roads.—At this time railroads purchase other roads or their stock, and incur expenses freely in the faith that they will be able to pay for it all at some future time; but when these obligations mature later on, the money market is likely to be exhausted from the many demands made upon it by business and stock market interests.

Wall Street market now speculative.—The Wall Street market now is likely to be a professional one, stocks being so high and the attraction of rising prices having ceased. The operations of professional speculators have little or no permanent bearing on the market, being mostly confined to certain speculative shares, and showing merely whether the

buyers or the sellers are at the moment in the ascendant. "Stocks now become wall flowers, and business does the dancing."

Stocks set aside by business.—"Bulls and bears" do not, as people think, always make prices. It is the times and conditions that are the main governing factors. As long as the public back them up, prices advance, but, having reached the limit, the public have now departed from the market and have left it to the manipulator. Stocks have ceased to rise, and both a commercial and a stock boom cannot be run successfully at the same time. Past experience has shown that the stock boom finally has to retire in favor of business, having had its day.

IX.—Latter Part of Boom Period

Business Increasing at Expense of Stock Speculation—About 13 Years after Commercial Panic.

[NOTE—*These conditions last occurred about* 1906. *If the next commercial panic takes place in* 1913, *for example, they may be expected to repeat themselves about* 1926.]

FROM two to three years after the financial panic Wall Street has again locked up a lot of money in stocks at inflated prices. Interest returns are lost sight of, hopes have been discounted and stocks of good companies yield less than their bonds. The banks are overloaned, the money is badly needed in legitimate lines, and business makes desperate efforts to get it back by forcing holders of stocks to liquidate. Stocks are now so high that they yield but small dividend returns, whereas commercial rates have been quietly rising and are now probably two per cent. higher than the average stock yields. Since money goes to the highest bidder, the fight is an unequal one, and stocks are doomed to defeat. This is indicated from time to time by spasms in call money, stringency

in time money, recurrent bank statement deficits, and violent fluctuations in stocks, whose values the manipulators and large speculators, now desperate, are trying vainly to uphold, despite the reaction which has set in.

Bull combines beaten.—"The slow attrition of bear attacks, the dribble of long stocks from tired holders and the accumulation of interest charges" finally down the bull combines, and a slow, quiet reaction in prices begins, notwithstanding the stubborn efforts of the bulls to resist it. Their promises have all failed and they are discredited prophets. The support that manipulators give stocks has finally become so self-evident, that it arouses the suspicions of the public and drives them away.

Stocks are now so inflated that they become water-logged and, like some old derelict on the ocean, are abandoned to the winds and tides of the financial seas, with but few to watch their wanderings. A high rate of dividend is not sufficient to support the price of a stock under these conditions, as was seen in the first six months of 1907, when stocks shrunk two billions, Union Pacific fell over 60 points, though paying 10 per cent. dividends, and similar declines occurred in Chicago & Northwestern, Great Northern, Northern Pacific, etc.

Bankers discriminate.—At this time, when the pressure for money is growing severe, bankers commence to discriminate in their loans against "wildcats" and all industrials, and this is perhaps one of the earliest signs of the coming change.

Improvement general; business takes money from speculation.—The improvement in general business, the growing steadiness in values, and the gain in confidence have, as we have seen, had a strong in-

fluence in drawing away capital from speculative employment. "Wall Street operations are founded on money—the surplus funds of the community at large; and when, to move his crops, to operate his mills, or for other reasons, the real owner of the money demands its return, Wall Street must comply and look elsewhere for capital." For a time, capital is obtained from Europe by paying high rates for the accommodation.

When agricultural and commercial demands become sufficiently great, they work along the lines of least resistance. They take money for their purposes from those sources from which it is easiest to get it, where it is in a semi-fluid condition already, and easily convertible. The most important of these sources is the stock market.

Rising prices give merchants the debt habit.—The stimulus to commercial enterprise and expansion resulting from high commodity prices and large profits, from having money or credits on hand, and from seeing friends making money, induces merchants and others to borrow more money than they have ever borrowed before and to run in debt further than is advisable—a habit that breeds trouble for them later on.

Steadily rising prices are sure, if continued, to appeal to the speculative side of man's nature, and to draw into the vortex of speculation people from all walks of life.

Each successive boom has a solid basis.—There is a legitimate basis for the boom in each kind of property, as it comes in succession, beginning with stocks and ending with realty. Each must show a handsome profit before being taken up. Thus the

boom in copper started in 1906 on a showing of 100 per cent. profit on every pound of copper mined.

Proof that speculation is rife.—A sure indication that speculation is in the saddle, accompanied by greater carelessness and waste in all lines of business, is now shown by an increase in the number of failures, with greater and more fraudulent liabilities. This period is marked by steadily decreasing cash reserves compared with bank loans and discounts. The cash is in hand-to-hand circulation, and later is used in the form of gold exports to satisfy foreign demands because of lessened exports of commodities. Extravagance of both municipal and central governments is another significant feature.

When loans exceed deposits at New York, the great money center, or the surplus is below the 25 per cent. required by law, it shows that banks are making excessive loans, or that they have themselves invested heavily in securities.

Car shortage on.—A car shortage is likely to appear, due to the excessive amount of freight handled, and when passenger cars are side-tracked, as is now sometimes the case, in favor of fast freights, it is an indication that the condition is becoming acute and congestion is threatened. This adds to the already stringent condition of the money market by delaying goods on the way to the retailer or material shipped to the manufacturer, thus tying up capital for the time and rendering collections slower.

New stocks and bonds yield better returns.—The railroads badly need new equipment, rails, and terminals. They issue new stocks and bonds to secure the required money, but these have to yield a much higher rate of interest to the investor than the old,

for they must meet the market rates. Their appearance in competition with other securities accelerates the fall of the older issues and tightens up the money market. Convertible bonds, issued at this time, are a concession made to buyers to induce them to purchase.

Higher interest rates indicate increased profits.—The rise in interest rates indicates the enormous increase in all lines of business. While prices are rising the higher rates are readily paid out of the large profits earned, but later, as profits diminish, the high rates become onerous and have to fall. Meanwhile, the craze for buying everything purchasable extends to the markets for household supplies and luxuries, and extravagance becomes general.

When to sell.—A writer gives the following as a good time to sell: "When the rise caused by excessively good times has gone so high that loans and discounts, after a steady and long continued rise, either become stationary for a period or else decrease progressively, coincident with a steady decrease in available funds."

Liquid capital turned into fixed.—Too great an increase in productive power in the form of factories, mills, etc., now taking place, is a useless duplication, and so changes liquid into fixed capital. This, however, is not as injurious to the world at large as if the capital were tied up permanently in a non-producing form and its usefulness thereby destroyed.

Increase in currency and gold.—A quiet inflation of the currency has been going on for some time past, stimulating speculation, extravagance and waste on all sides. The gold we import from Europe now, instead of going to strengthen the gold

reserve, is often used to prevent the liquidation that nature is trying to enforce, or to inflate prices still higher that are already too high. This inflation and that caused by war have often been mistaken for true prosperity, instead of being recognized as an unduly stimulated condition, that must be paid for later on.

Government surplus.—As the volume of business increases the demand for money grows with it, until the attention of Wall Street (Wall Street first, because at the time it is most in need of money, and because it is the great market for money) and later on the attention of the merchant, are called to the large amount of idle capital in the government's possession. They demand that this idle fund shall thereafter be lessened. This gradually helps beget a tariff agitation, which becomes more insistent as business profits are narrowed down—even though the surplus may in the meantime have turned to a deficit. Tariff revision generally results, which in itself is always unsettling. It first affects business lines, and some time is always required to readjust credits. In consequence many writers have ascribed this as a cause of panic, rather than as an effect produced by other and greater causes.

Banks overloaned.—When banks overloan, they often, instead of reducing their loans, take out new circulation, and attracted by big interest rates, loan this money out in order to increase profits, instead of keeping it in their reserves.

Scarcity of labor injures business and railroads.—The great scarcity of labor that has existed—two jobs for every unemployed man—has been a material factor in increasing costs; for not only is labor scarce, but its efficiency or producing value has

fallen off considerably. This affects all lines, but particularly the manufacturer and the railroads. The New York *Herald,* June 24, 1907, quoting Frank A. Vanderlip, President of the City Bank, says: "With the advanced wages of the last three or four years labor has on an average shown a decreased efficiency of 20 per cent."

Inflation breeds further inflation.—An increase of prices caused by inflation calls for still further inflation, as it takes more money now to do the same amount of business.

As values continue to rise they finally reach a point where the wage earner and the man with a fixed income are at a disadvantage, and the owners of commodities, real estate, etc., have, because of the inflated prices of their property, a decided advantage.

Purchasers do not buy as eagerly as formerly in anticipation of their wants. There is not the money in it for the purchaser that there was, as prices are not rising as they formerly did. This indicates that the top is nearly reached.

Dividends increased to offset higher interest rates.—When business increases in boom times and interest rates are high, in consequence of the great demand for money, so that it will not pay to hold high priced stocks yielding small returns on the investment, there is an endeavor on the part of those in control to meet the emergency by raising the dividends of stocks so far as it is possible, with an idea of selling out to the public; but this can only be done in isolated cases, and is not effective in stemming the falling tendency of stock values due to lessened money supply. A great deal of formerly liquid capital has by this time been converted into

fixed values, and the demands of business are now greatly increased by high commodity values, etc. All want more than they can get.

Bonds and stocks sold to get money to loan.—Bankers and others gradually sell their stocks and bonds, attracted by the higher interest obtainable in the money market, as overproduction and exaggerated prices compel recourse to credit. A period of dear money is in full force.

Masses overdiscount the future.—The sanguine temperament of the masses during a boom leads them to overdiscount the future, so that when the results are accomplished they are apt to be disappointing, and a small fall in prices occurs, unless the results exceed the greatest estimates.

Generally wrong to increase money supply in a stringency.—Increased trade activity and speculation (to which there can be no limit, except through the money market) have absorbed the greater gold and currency output. For years, and even at present, the erroneous idea, in boom times when money becomes stringent, has been to increase the supply of money no matter how badly inflated it may already be; instead of allowing natural laws to work and force a liquidation that will bring prices and business down again to normal conditions. This always has the effect of driving out foreign capital and causing shipments from Europe of our stocks, bonds and evidences of indebtedness. It sows the seeds of distrust at home also, producing a curtailment of operations and a drawing in of capital. The measures we take should always be of a kind to assist nature, not to oppose her.

Many spend more and save less.—The masses have spent more and saved less than they do under

quieter conditions, and many go so far as to capitalize hopes and spend freely on the strength of it. With boom times comes to many of those who have succeeded beyond their anticipations, a desire for luxuries and self indulgence, which begets selfishness and greed and so warps their minds to the rights of others that it weakens the foundations of integrity in business as well as in social life. The hosts of desires that spring up clamoring for the means of indulgence, call continually for more and more money, and hence the disgraceful disclosures that show up so plentifully when bad times set in again.

We strain our credit to maintain prices.—In our eagerness for money, to meet the demands of business and our own inflated plans, we seek it in the lowest market, and hence at this time always accumulate a large foreign indebtedness. We keep on borrowing from this source until we have exhausted foreign loanable funds, or until the limit of our credit is reached, or both. Especially is this overstraining of our foreign credit applicable to our railroads and to Wall Street speculators, the latter using it at first to raise and now to sustain inflated prices, to the detriment of everyone, themselves included.

The greater the rise, the greater the reaction.—The longer the period of uninterrupted prosperity and activity and the greater the pace, the surer and greater is the ultimate reaction; but no one cares to entertain such thoughts at present, for everything is booming.

Excessive interest rates contribute to high prices, as interest enters so heavily into cost. During the boom, manufacturers, railroads, etc., lose sight of

economy in the rush to secure orders or to deliver on time.

Increase in incorporations indicates large business.—The turning of private business into corporations and the formation of trusts is one of the signs of inflation. It indicates a larger business than individuals can carry on to good advantage, and also a desire to produce goods cheaper and to wield more power, and sometimes to control the market if possible. It allows of bank loans on stock, and so opens up a larger line of credit. This is not a bad feature in itself were it not that the stock is frequently inflated, and often promoters are able to secure the services of bankers to assist them in the flotation of their stocks at exaggerated values.

Improved methods increase gold output.—New chemical and engineering methods and a larger supply of available capital are in a measure accountable for the greatly increased gold output and for a large part of the increase in ratio of wealth in the United States to population.

Developing our magnificent resources.—Another cause is the tremendous resources of our magnificent new country. Our rapid increase in population; our quickness to create and use labor-saving devices, making labor so much more productive; our freedom of government and of the conditions of labor; our great and beneficial mixture of nations; our varied climate and the great area of our country, where unhealthy crowded conditions, as in Europe, do not exist—all tend to make the United States experience a greater degree of prosperity than Europe, and consequently a greater reaction. The extreme swing one way roughly measures the return, as in the movements of the pendulum.

The West and Uncle Sam.—The West is now using considerable money developing her great natural resources, and is calling upon the East for its surplus funds, so adding to the stringency of the money market in the East. Uncle Sam is also adding to this condition, for as the times improve his income grows larger and he has a greater surplus locked up in his vaults, that is badly needed in business. Later he has to come to the assistance of the money market.

Features of the times.—When great increases in clearings in interior towns continue, with no corresponding increase in quantities of goods moved or marketed, it means that speculation is spreading, conditions are unhealthy and legitimate business has ceased to expand. The trunk lines indicate this condition best, as they carry the harvest and return laden with commodities. Bank clearings are now deceptive, as they may indicate a larger business due to excess of speculation, when legitimate business may be halting; and also because it now requires much larger clearings to transact the same amount of business as formerly, because of high prices.

Very high and fluctuating rates of interest on 'change without apparent cause (as in Dec., 1905), are apt to be due to overexpansion of credits, and often for the use of an already inflated stock market.

Commodity prices go up so high, after a long period of good times, that the wage earner cannot save as much, and the savings banks (having less deposits) consequently buy fewer bonds and stocks.

Public leaving stocks.—The stock market is now constantly being deserted by the public, as not only do they need the money for other purposes, but

many realize that the long continued bull market has finally reached the point (as it always does where success has been long continued) where prices represent not only actual values but capitalized future hopes as well, and stocks yield much less than interest and therefore are unsafe.

Quiet decline in stocks first.—This condition has started a quiet decline, hardly noticed at first, but continuing despite the fact that nothing has happened to injure the position of the railroads or other industries. Earnings continue phenomenal, bank clearings the largest ever, and all departments of the nation's activity appear to be in fine condition; but interest returns are unsatisfactory and business needs money, and there is a shortage of it because of overexpanded volume of business and speculation.

Diminishing bank reserves.—Excessive loans and underwritings by bankers on rapidly diminishing bank reserves are another feature of the abnormal pressure for funds.

The securities market is eventually governed by the money situation, no matter how hard the manipulator and others may at times try to avoid that result.

X.—Stock Boom Ends First—Business Now Affected

About Fourteen to Sixteen Years after Commercial Panic.

[NOTE—*These conditions last occurred* 1907-1909. *If the next commercial panic takes place in* 1913, *for example, they may be expected to repeat themselves about* 1927-1929.]

WHEN stocks are excessively high and bank reserves dangerously low and obligations continue to increase, it is only a question of time when the penalty is paid through the enforced liquidation of stocks. This may or may not be accompanied by panic conditions, depending chiefly on the degree of confidence entrusted in the banks at this time. The bank reserves must be replenished when below the safety limit, and must be put on a safe, substantial footing as soon as possible. Nature's way of doing it is through liquidation.

Man, from time to time, has tried other methods of solving this question, such as inflation of cur-

rency, etc., but at best these are only temporary expedients, leaving the situation finally worse than it was before. The speculator can always use funds faster than they can be supplied to him, and if the process is continued, doubts arise as to the stability of an inflated currency. These fears increase and finally kill all confidence and so close up all avenues of business, and gloom and depression then rule in the financial and commercial worlds.

Liquidation in stocks.—The fall in stock values, which has been in progress for a year, still continues, followed later by stagnation. Prices will not rise again until the inflation of credit has passed by, and money becomes plentiful by reason of lessened demands for it (as late in '08). When that time comes, interest rates fall to a minimum, so that capital yields small returns in the money market; and stocks in the meantime have fallen so greatly, that dividend returns on the latter compare favorably with the small interest yields in the money market.

Consolidations beget distrust.—The consolidation of existing manufacturing and business houses (purchased at extravagant figures, perhaps) into one large corporation, capitalized on a sufficiently liberal basis to yield great profits to the promoters, assisting bankers and guaranteeing syndicates and also to allow of the sale of the stock at what appears to be a liberal discount to the confiding public, makes the future of such a corporation very problematical to say the least. When these consolidations have been effected in many industries and branches of trade and many new corporations have been formed, a feeling of distrust is engendered which helps to start a fall in values, first in these new untried

shares and then spreading through the entire list, not sparing even those which make an increased dividend showing.

Recapitulation of progress of events.—The progress of events is as follows: Prosperity ushers in an era of money making, evidenced by a rise in values, by increased bank clearings, growth in the traffic and revenues of transportation lines, lessened mercantile failures, car shortage and scarcity of labor, higher wages, consumption outstripping production, and a general feeling of confidence; these carried to an extreme result in overproduction (as compared with present needs), unwarranted speculation, extravagance, and excessive prices; then comes a fall in values, exhaustion of capital, and fear, ending later on in panic.

We are now very sensitive to foreign conditions.—Borrowing heavily from Europe as we now are and have been for some time past, our markets are very sensitive to anything that affects Europe financially, fearing the loss of that market to borrow from. Undue borrowing abroad, like undue inflation of currency, provokes extravagance, begets great credits and eventually undermines public confidence. The country is plunged into debt for luxuries, a foreign balance accumulates against us, and the day of reckoning surely follows. These conditions now exist.

Banks supply capital to manufacturers.—In boom times so great is the volume of business done that manufacturers often have to apply to the banks for loans to supply temporary working capital, much of their own capital having been absorbed in permanent forms, as in factories and the like. Thus banking conditions quickly react on business.

High interest rates eventually wear out speculation.—A high rate of interest long continued, will in time wear away any speculative movement, and if continued unduly will seriously affect business operations; and when business is on an inflated basis as at present, the injection of the element of fear, especially if directed against the banks, will, if the financial tension is not relieved, bring on liquidation and perhaps panic.

Pools operating now.—Pools and cliques now operate on the stock market where individuals used to. They find it a difficult proposition to finance their deals, and equally hard to keep up prices of their favorite stocks.

Banks borrow at home and abroad.—Many banks have borrowed out-of-town funds at high rates of interest and have used the money to help promote speculation. These borrowed funds form the basis for enormous loan expansions. The banks also borrow from abroad to bolster up their reserves and to aid further expansion. The result is that later on our exports have to go toward settling up this foreign indebtedness instead of easing finances at home.

Western banks sold stocks first.—Even before Eastern banks were forced into selling stocks the Western banks had done so, as their relations with the stock market were not so intimate, and the demands of business in the West, owing to the great development work there, were even more urgent than in the East.

Syndicates and new securities out of favor.—"Syndicates, formerly hailed with delight, also new securities, become a source of alarm and give Wall Street a chill," and are now abandoned as failures. For a time they are floated in Europe, as a last

resort, at a higher rate of interest; but as American conditions become better understood abroad, and as conditions there also become poorer, the foreign market for new securities also fails.

High prices increase imports.—Prices are so high now that many foreign goods are sold here despite the tariff wall we have erected; and foreign purchases, discouraged by our high prices, fall off, so that exports decrease in many lines while imports, owing to our extravagance, are steadily increasing. So at the same time we open wider the flood gates of the world's competition, and diminish our own resources to pay with—a decided step onwards toward hard times. Later we attempt to shut the gates but find it is too late, for the damage has been done.

When maximum of employment and business activity.—I quote from Burton on "Crises," pp. 183, 89, 153: "The maximum of employment somewhat precedes the date of the highest prices and frequently precedes the maximum of production."

"In the period of exhaustion preceding a depression imports will be very large, and will bear an unusually large proportion to exports."

"The greatest degree of prosperity is some time before the breaking out of the crisis or commencement of the depression."

Maximum of imports and activity compared.—"In a debtor or developing country, the maximum proportion of exports to imports occurs at a considerably earlier date than the maximum activity (generally two years), and indicates that the greatest amount of business activity is contemporaneous with the maximum of consumption rather than with the

maximum of production. It indicates that the people are spending freely."

Government deficit apt to occur.—As times get poorer government revenues fall off rapidly, especially as goods now accumulate unsold, many of which have been previously purchased in hopes of a demand which does not materialize. Finally a government deficit occurs and a new tariff may become a necessity to replenish the exhausted exchequer. If so, instead of a revision downward, it results in an increase in rates, much to the disgust of the public, and to the loss of prestige of the political party in power.

Overprosperity breeds adversity.—A condition of exceeding prosperity germinates and nourishes the seeds of adversity. It begets overconfidence, recklessness, overextension of credits, overdoing in all lines of business, greed, corruption and extravagance—qualities exactly the reverse of those which caused the good times. When corporations and municipalities have set the example it is no wonder that such conditions have gradually permeated. all lines of business.

International fight for gold.—When prosperity is at full tide the active commercial nations are all using a good deal of money, and an international contest, as it were, for gold sets in. Each nation tries to retain the gold it has on hand and to acquire as much more as possible. The most successful in this contest are the most progressive nations, with the largest resources in the most active stage of development. These are the bidders that can afford to pay the highest price and so secure the coveted gold. Sometimes the price proves ruinous in the end.

Increased failures among manufacturers show lessened profits.—For some time after prosperity has reached its height the falling off is not clearly perceptible in the volume of business done, but the risks of business grow greater and the margin of profit is less. Competition becomes so active that net results grow poorer. This does not come until the working capacity of manufacturing and business plants has been greatly increased. Up to that time there has been more than enough for all, and hence no need for active competition—no necessity to hunt for orders which were clamoring to be filled. This condition of lessening profits is shown by the increased number and amounts of failures among the manufacturers, which indicate the presence of both speculation and excessive competition.

Hard to be honest now.—Human nature finds it very hard to be strictly honest in times of feverish speculation and overtrading, with extravagant habits and desires clamoring for gratification and the money in hand for the purpose. When the reaction sets in, many find it a struggle to maintain their financial standing. As a consequence, a condition of financial rottenness shows up just before and for some time after a panic, that is most deplorable, and is one of the agents quietly at work sapping our confidence in values and in men, and so adding later on to the panicky and depressed feelings of the public.

Neither labor nor capital fully prosperous now.—Neither labor nor capital at this time enjoys the full measure of prosperity; they are both subject to the law of compensation and both have to pay higher prices for everything. Toward the end of good times the margin of profit grows smaller, indi-

cating growing competition, and that the cost of articles is advancing faster than the seller can raise his prices to the customer.

Greater sale of cotton goods.—When the wage earners and those with stated incomes curtail their purchases, a relative increase in the sale of cotton goods is observed, as they are necessary staples and cheap, while sales of silks and woolen goods, which are higher priced, fall off. Likewise automobiles and diamonds are in less demand.

Why inefficient business men have succeeded.—Under modern conditions large profits in business are realized only for a short period. Competition is active most of the time, and the margin of profit is generally small. Close attention to business and to small savings are necessary to success. But the period now just passing has been exceptional. The demand for goods has been so great that many who would not have the qualifications to succeed at other times have done well; but their speculative and overtrading methods come to grief later on, and greatly swell the list of failures. The test of declining values and keen competition proves too much for their loose and speculative business methods.

Railroad financiers are shown preference over merchants.—The railroad financiers, doing a very large business through banks in placing their stocks, bonds, etc., naturally are closely allied to the great banking interests, so that merchants are apt to complain from time to time of the preference shown to the railroad as against the merchant in the extension of credits.

Prices rise faster than wages.—Prices of commodities and rents advance faster than wages, so that

towards the end of the prosperous period and thereafter the poorer classes complain. In New York, especially, meetings are likely to be held denouncing butchers and landlords and small riots may occasionally occur. Still later, when prices become higher than workmen can stand they may even call the boycott to their aid.

Car shortage.—Car shortage, now at its most acute stage, works considerable damage to the business interests of the country tending to restrict output and to compel the idleness of more or less capital. Perishable freight, of course, suffers the worst of all.

Money still for Wall Street but conditions unhealthy.—During these years money still pours into Wall Street, at intervals, from all over the country, to take advantage of the high rates of interest offered—rates that are bound soon to fall, as they are prohibitive to all non-speculative lines of business. In our last boom several of the banks and trust companies in New York City paid as high as four per cent. to get out of town deposits to help maintain inflated prices, and these prices formed the basis for a further great expansion of loans. Frequent spasms in the money and stock markets emphasize the feverish and unhealthy condition of affairs, and the desperate efforts being made to resist the continued fall in stocks.

Why merchants now sell their stocks.—A falling market and high interest rates make merchants who need the cash sell their securities rather than borrow at exorbitant rates. This adds to the liquidation. "It is a law that speculation will run its course until it devours [or frightens] capital," and both events are now occurring; also that "the vul-

nerability of a speculative market increases as prices advance" and more and more capital is thus tied up.

Great increase in municipal indebtedness.—The increase in municipal indebtedness during good times is something enormous, and goes on so quietly throughout the country that no one has any idea of the extent of it until the panic comes. Afterward, many municipalities have, in past cycles, ceased payment. Thus the Philadelphia Social Science Association in its reports 1871 to 1879, estimated that in 1873 the cities of the United States owed one billion dollars, on four hundred millions of which payment of principal or interest was stopped when the panic of 1873 came on. The same authority figured that by 1877, of the 2,200 million railroad bonds, one-quarter had defaulted interest; and of two billions in railroad shares, three-quarters in the East and four-fifths in the West paid no dividends, and all the roads had to retrench and reform. Fortunately, however, for us, our railroads have now passed the experimental stage and the territory through which they run is fairly well peopled, so that such a deplorable showing is not likely to occur again. We may hope that municipalities also have been taught a lesson, and that hereafter they will not plunge so deeply into the quagmire of debt.

Excessive prices hurt small dealer.—During this period every great advance in wages and commodity prices injures the small dealer, as it demands more money of him to do the same volume of business with, besides lessening his gains and so compelling him to do more business if he wishes to maintain his usual inflow of profits. If he attempts to raise prices as a last resort, his sales fall off. Moreover,

such a condition is likely to entail a greater loss of perishable goods, and also in bad debts.

Prosperity passing.—Great prosperity, with all its excesses, is now about to pass away, to be supplanted eventually by the other extreme. There are two things that must be taken into consideration in comparing the good and bad features of great prosperity, which are not shown up in figuring mathematically on the rise in wages as against the rise in commodity prices. One is the increase in the number of establishments in which certain kinds of labor are employed, and the consequent greater chances for advancement; as exemplified in the evolution, during good times, of the house servant into the factory girl, the office boy into the stenographer or clerk, etc. Yet notwithstanding this, the consensus of opinion among those who have studied the subject is that the wage earner in boom times does not get his full share of the benefits arising from the great activity in all lines of business. But it might here be added that the compensation of labor has been steadily increasing from the "good old times" (so called) in England, when the laborer's reward for a day's work was only a penny or two, and that often thrown to him with a curse.

Business men incur indebtedness.—As one writer says, in good times many of the railroads and business men seemed to be engaged in piling up obligations, which they meet with a smile when times are good, but which bring the sheriff to the door when bad times are in the saddle. Another said in 1864 that the people were hopeful, extravagant and in debt. In fact, the economic waste of boom times is only exceeded by the ravages of war.

Railroads offer short time notes.—Railroads now

find the rate of interest so high that they cannot afford to issue long time bonds on such a basis—a policy which past experience has shown often results in ruin. They now offer short time notes instead, bearing a high rate of interest. These supplant the long time bond for the time being, as they are more attractive, running for a short time only and bearing a higher rate of interest. But money becomes so very scarce that it is difficult to float even these in any considerable amounts. Later on, when business is waning and money is thus released in large amounts, these notes, being somewhat dangerous as floating liabilities, besides being very costly, are replaced with long time bonds bearing more reasonable rates of interest.

Syndicates terminate with a loss.—Banking and promotion syndicates may, under present circumstances, find it impossible to sell stocks or bonds, and they often terminate by dividing up the loss and the stocks or bonds on hand, because of sheer inability to secure the necessary funds to complete the operation.

Increase in mortgage indebtedness.—When the increase in mortgage indebtedness grows faster than the increase in realty values it is a bad sign, for it is real estate and mortgage indebtedness that weighs most heavily on the public in times of panic and is the hardest to get from under.

Credit will not always take the place of capital.—"No matter what book profits a country or business may show, prosperity cannot continue with steadily increased expenditures, without a corresponding accumulation of capital. Credit will take its place for a time but there is a certain end to that."

Thrift is begotten in the school of hard times.

Continued good times lead us to forget these lessons, and they can only be taught again by a return to adverse conditions.

Builder for profit first to stop when materials too high.—When materials get too high, the first one to discontinue operations is the builder who is building to sell again. It is his profit that is absorbed by the excessive rise in building materials and lots.

As capital becomes fixed, interest rises.—Trade and stock activities have now outrun the point at which they can be financed. Liquid capital has been greatly overworked and in part disappears, and as it grows less the use of the diminishing balance commands a higher and higher rate of interest, until the rate becomes prohibitive to the successful carrying on of business. Finally the amount of capital offered is so small that it is practically unobtainable, thus forcibly checking further expansion.

Railroads and other companies retrench.—Railroads and industrial companies, finding money practically impossible to borrow, issue as few bonds or notes as possible, and so gradually lessen the demand for money. They soon discharge workmen, and confine their expenditures to those absolutely necessary for the maintenance of the road or already contracted for, and this is one of the first great checks to prosperity.

Realty movements.—The action in real estate varies in point of time in different parts of the country. An advance in rents, sufficient finally to make it cheaper to build than to pay rent, starts very quietly what might be called a consumptive demand. This first sets in some years before, shortly after the financial or securities panic. It is a demand for houses and lots for use, and has no ele-

ment of speculation in it. The lots are bought to build houses on, and only lots for this purpose are salable.

In the East, especially in parts of New York City —which is the money center, and whose population is increasing rapidly, not only by births but also by the incoming tide of immigration—this movement may begin even before the securities panic. Other cities follow, especially those where the tide of immigration has been flowing for some time past into the city and surrounding country, and those which the newspapers have widely advertised. The population of Los Angeles, for example, is greatly augmented by well-to-do tourists who locate or visit there in large numbers, and have money with which to buy. In such localities the boom flourishes and runs to a finish (excepting certain parts of New York and suburbs) earlier than in the greater part of the United States—like the Central West, which has of late had no particular advertising or exceptional increase of population, but has moved along quiet, home-building lines only. These latter sections, while experiencing a betterment, do not experience a real boom until more favored localities have ceased to move, or even later, when general business may be on the wane.

Bank deposits show decreases.—"When bank deposits begin to show decreases during boom times, it is an indication that these deposits of credit, as most of them are, are gradually ceasing, due either to compulsory measures on the part of the creditor, or to the fact that people prefer to pay their notes rather than to seek new investments, or both. This change always marks the beginning of a decline in the price level."

Abandoning of new enterprises shows less business.—As interest rates have now become too high to permit the launching of new enterprises at a profit, they are consequently abandoned; and this is one of the noticeable signs of unhealthy business conditions.

Enforced economies.—When prices have gone so high that people living on a fixed income and the wage earning class cannot pay them, the only thing left to do is to curtail the expense account by lessening purchases and buying cheaper articles. This marks the end of the good times period. The result is felt immediately by the manufacturer in a loss of orders, and he has the alternative either to increase his business or to reduce his prices. This latter is very objectionable to him, as at this time he has not yet been able to raise his prices sufficiently to meet the last increase in the cost of raw materials and labor; nor does he wish to discharge valuable help that he may need in the future, as he is still hopeful of better conditions. Consequently he elects to do a larger business, if possible, even at a smaller percentage of profit. Thus, when the masses are forced to curtail purchases, competition sets in for the lessened business in sight and merchants suffer severely; but not as much as still later on, when falling values turn profits into losses.

Money stringency and perhaps panic.—It is at this time, when the culmination of high prices has been reached and reaction sets in, when business has begun to decline and railroads have been forced to curtail their operations, that the supply of ready money becomes so limited that a great money stringency occurs. If the strain on the money market is too great, and fear of the banks' solvency be-

comes wide-spread, credit will be suddenly curtailed, and a run on the banks takes place. Hoarding ensues, and a money stringency panic is on—the most severe by far of all the minor forms of panic.

Such a panic occcurred in December, 1907, and came close to occurring in 1867 and 1887. It is doubtful, however, if there would have been a real panic in December, 1907, had it not been for the fact that several of our old New York banks and trust companies had come under the control of rash speculators. For this reason the financial standing of these institutions in the minds of the public became so weakened that with the approach of stringency came fears of their stability. Rotten disclosures had been gradually coming out for some time previous and the great moneyed powers saw the absolute necessity of eliminating irresponsible speculators from the control of important financial institutions. This aim could be acccomplished at this particular time by merely refusing to extend aid to them. The fact that Morgan and the New York clearinghouse banks stopped the panic after it was under full headway showed plainly that they could have stopped it at the start, had they really desired to do so. This was done in 1867 and in 1887 when the strain came, although the banks were then comparatively weak and not united, whereas now they have not only learned to act in unison but their power to carry out their designs is almost inconceivably greater. Such a panic as 1907 is not likely to occur again for the same reason, as the consolidation of great banking interests that has been going on ever since and the lesson already taught will probably prevent outside speculators from again at-

tempting to gain control of banking institutions of any great importance.

Money stringency at this point in the cycle occurs, luckily, at a time when past profits have been large, so that the people are able to stand the strain.

Liquidation necessary.—Liquidation is a necessary prerequisite to the progress of convalescence. It is a readjustment of values on a lower basis and must go far enough to relieve the great money strain; but, working under the law of action and reaction, prices will go as much too low as they went too high previously. The liquidation is apt to be started by some prominent event, if coincident with the period of change. Thus speculation was temporarily halted in 1881 by Garfield's assassination, and in 1901 by President McKinley's.

Review of events leading up to panic of 1907.—Commodity prices in 1907 rose to the highest point since the Civil War, creating, with speculation, an excessive strain on credit. Commerce had increased 2600 per cent. since Jefferson's time but securities had multiplied a thousand fold. Morgan had purchased the steel interests for 300 millions—a most exorbitant price, many thought—and had capitalized them for a billion and a half. H. H. Rogers had turned forty millions of copper interests into a veritable flood of securities. Heinze had sold Butte Coalition to the Standard Oil Company for eleven millions and they had capitalized it for forty millions. Much of this stock was sold to the public, who were easily induced to buy, under the excitement of boom times, when men with names of great financial prominence engineered the operations. J. J. Hill issued 150 millions of new securities against ore lands in Minnesota. Ryan had issued millions of traction

securities, and the Metropolitan Street Railway Company went into the hands of a receiver.*

In 1907 alone $2,102,555,000 in new securities were issued, for it is far easier to create new securities than it is to supply new money. The liquid capital of the country necessarily became greatly diminished, and we suffered the consequences of inflation in security, commodity, labor and realty values, and the excessive speculation that accompanied it. The wonder is that the collapse did not come before, especially when we realize that some of our banks and trust companies were under the control of reckless speculators. In fact, fear of the methods of one of the several who were later indicted, was the cause, in 1907, of the failure of five of our best financial institutions—among them one of the oldest in New York, which had been a pillar of strength in previous panics.

Panic bound to come.—The elements were all there, and a panic was bound to come. Indeed, it was fortunate that it came when it did, otherwise these speculative bankers, operating, as they would have to later, on a falling market, would necessarily have plunged deeper and deeper into the mire, and would perhaps have acquired control of bank after bank to prop up their falling fortunes, so that eventually a dozen Morgans and Rockefellers could not have controlled the situation, and we would have had the worst panic that the world has ever seen.

Not a true commercial panic.—It takes a long period of declining profits, shrinking stock and commodity values, losses and debts to make a lasting panic. Panics like 1907 are to be classed as financial rather than commercial panics like those of 1873

*Wall Street Journal, Dec. 16, 1907

and 1893. The financial panic does not clear up the atmosphere like the commercial panic, by reducing prices in general and checking extravagance for years thereafter.

A sharp rally from this panic.—Later a rally sets in, business is better for a time, and plenty of cheap money enables rich manipulators to raise stock prices to an abnormal height, hoping thereby to induce the general public to come in and buy—which they never do, however, to any great extent. Commodity prices also rise again, if the crisis occurs before prices have reached their limit; and if good crops are garnered business is better, especially with the railways, owing to the great reduction in their expenses, as well as to better business. The merchants, however, especially the retailers, never realize again the former boom profits. Confidence has been shaken and losses have been too heavy, and the excessive cost of goods does not permit the retailer to charge the buyer the usual per cent. of profit.

Competition among retailers.—At this period the retail merchants complain considerably; for while the volume of business is large, competition among the smaller merchants reduces greatly the business done by each individually. When times were good many, incited by the sight of others making money, went into the retail business. Others went into business because high prices reduced so greatly the purchasing power of the interest received from their investments that they had to do something to augment their incomes. Especially is this the case when prices remain high and interest rates become low, during the depression. Therefore at this time we find the retail business overcrowded and net profits comparatively small, while the wholesalers

are doing a good business. The competition of increased numbers in their lines is not nearly so severe as among the retailers, owing to the larger capital and greater experience necessary to embark in a wholesale or manufacturing business. Later, however, increased numbers affect these lines also.

Stocks again weaken.—Stocks are the first to fall again, as at this time the public are not purchasing and stock prices have been unduly raised by manipulation, operators having taken advantage of the cheap money rates following the reaction to force up prices on borrowed money. The great increase in imports, due to extravagance, and the relative falling off in exports because of the prohibitive prices of many of our exportable products, results in exports of gold; and, because of the greater demand for money due to business improving after the crisis, bankers call in many of their speculative loans. This once more pulls the money prop from under the market and a reaction in stocks begins.

XI.—Business Declining

Accompanied by Competition and Lessened Profits, also Falling Values and Wages. About 17 to 18 Years after Commercial Panic.

[NOTE—*These conditions prevail as this book is written*, 1910. *They may naturally be expected to continue, in a general way, through* 1911.]

IF a panic occurs when the crisis is reached, as in 1907, stocks, about a year after, will have rallied under the skillful manipulation of large operators, who, with low interest rates to help out, will once more be in the saddle; but this is only temporary and a downward movement sets in. This commences when our heretofore favorable foreign trade balance is so greatly diminished—by reason of the prohibitive prices of many of our export products, and the extravagance of purchasers of imported articles, resulting in increased imports and lessened experts—that gold has to be exported in large quantities to pay our foreign obligations. For a time the exchange market is kept partially in hand by foreign borrowings; but the drain of gold finally

compels bankers to lessen their loans to stock speculators. This results in the gradual withdrawal of support from the market and in quiet selling on every bulge, so inaugurating a downward movement in stocks.

Course of liquidation.—This liquidation is eventually to extend through all lines of business, in substantially the following order: First, shares of corporations, then raw materials, then manufactured goods at wholesale, next goods at retail, then rents, and finally real estate values. Ready money is overworked and credit becomes exhausted, the latter being expanded out of all proportion to the gold reserve, and fear, that graveyard of prosperity, is beginning to make itself felt. Especially is stock liquidation great at this time if scandalous disclosures come to the surface, as is apt to be the case.

Cliques and investors now own stocks.—Stocks are now mostly held by big speculators and by the investing classes. The former bought stocks from the original owners, mainly on the strength of bank credits, in order to sustain prices. Such obligations they have to pay up to their now anxious bankers. The genuine investor buys stocks at what he considers bargain prices with his ready cash, and of late years the number of small investors who have taken advantage of sharp declines to buy has greatly increased.

Banks overloaded with securities.—But there is still a great mass of undigested securities in the hands of underwriters, and other first holders. Banks also are often laden with securities that the public does not want, and hence are not able to give satisfactory assistance to their merchant clients. The banks now have to refuse to finance new companies

or consolidations of any kind, and finally they are compelled to limit credits greatly because of their growing fear as to the solvency of some of their customers, and because of gradual withdrawals by depositors from the banks, thus lessening their average balances.

Liquidation gradually extends to commodities.—When the decline in stocks began business was active and remained so for some time thereafter, but the trouble is plainly seen in the money market, and if the supply of ready cash remains inadequate after the fall in stocks, liquidation then extends to commodities and affects general business, inaugurating an era of retrenchment and saving all along the line.

Reduced railroad buying.—As railroads are the heaviest consumers in many lines of industry, their greatly reduced purchases seriously affect the activity of general business.

High prices have checked consumption.—High prices, having reached the limit of many of the purchasers' ability to pay, have checked consumption. This hastens the accumulation of a surplus in production, and thus a fall in prices—the result of excessive competition, oversupply and underconsumption; and finally the resulting falling off in production decreases, in a measure, the urgent call for money.

Easier to manufacture goods than to get money.—Since the introduction of modern machinery, it has always been easier to manufacture goods than it is to secure the necessary money to finance the output. The withdrawal of a large body of purchasers at this time expedites the process of liquidation.

High interest rates, high priced and insufficient

labor and dear raw materials reduce profits; and, with a money stringency, are now quietly stifling most new enterprises and making it more difficult to continue old ones.

Who discharge help first.—During money stringency many of the first to discharge hands are manufacturers who are doing a very large business and who cannot secure the necessary ready cash to pay running expenses, especially wages. Suspensions and failures occur at this time in greater numbers among manufacturers than in any other class, and especially among those who are financed in the East, where the money stringency is greatest.

High prices and interest lessens gold output.—It may be noticed in passing that excessive commodity prices and high priced money and labor eventually make gold and silver mining less productive and lessen the output by shutting down many low grade mines. In time this becomes a factor in again lowering commodity prices and reducing wages; but the operation of this influence is slow and extends over a period of years.

Long continued prosperity begets indebtedness.—A long period of prosperity begets a large volume of new indebtedness, which finally grows so great, prior to and at this time, that it helps gradually to break down credit and force liquidation. "Credit demands a rock basis to rest on," and where this basis gradually changes to the shifting sands of dishonesty, debt and speculation, the destruction of credit follows and liquidation sets in.

Movement from city to country.—Excessive commodity prices force many from the city to the country, there to become producers and thereby eventually to lessen the prices of commodities. This move-

ment assumes large proportions as the times grow harder later on.

When want of confidence begins.—Want of confidence sets in when prices are so high as to raise doubts of their permanency, and when there is a lack of money and credit to do business on; and this occurs when the overdoing of business and speculation cause a money stringency, for no amount of money and credit can satisfy the demands of speculation.

Bank credits and prices.—Contraction of bank credits acts in exactly the same manner as a contraction of the currency in producing a fall in prices, and this fall in prices, creating distrust, makes it harder to get bills discounted and so works for lower prices still.

A few prepare for what is coming.—A few far-sighted business men, anticipating the general trend of events, now refrain from speculative enterprises and prepare themselves for whatever change may be coming.

Prices decline before production.—Prices decline before production; for when the price of an article advances, production will increase until demand lessens or overproduction takes place and prices decline. Retail prices fall more slowly than wholesale.*

Iron and steel a barometer of trade.—The iron and steel trade, being so vast and its ramifications into other lines so great, is generally accepted as the barometer of trade. In dull times it feels the reaction more keenly than any other business, as orders have to be given six or eight months ahead, and these are often cancelled if conditions appear un-

* Burton on Crises, pp. 48 and 170.

favorable. Many of these orders are in the nature of options, accepted on the faith that they will probably be wanted, and sometimes given in order to secure precedence of delivery when needed later. This liability to cancellation occurs in other manufacturing lines (although not to so marked a degree) and consequently may change the business aspect for the worst at very short notice. At this time iron and copper suffer especially, as they enter so largely into new construction and new construction depends on new investments, which have practically ceased at this period.

Interest rates fall with commodities.—It should be borne in mind that during a slow and long continued fall of commodity prices, interest rates will decline, so as to offset, at least in part, the gain in purchasing power of the principal, thus tending to maintain a proper equilibrium. Also, as profits decrease in business undertakings interest rates will fall, for the latter depend on profits and must, in the long run, come out of profits.

Speculation shifts to commodities.—On the other hand, when speculation in the securities market is dull, we often see traders shift their operations to the speculative commodity markets—grains, cotton, pork, etc. After the defeat of stocks in the money market, speculative capital is no longer attracted to stocks, but seeks activity on the produce exchanges, where commodities are most readily bought and sold and where values are less intimately connected with the rate of interest.

Realty next.—These speculative commodities gradually become less inviting from being over boomed. Meantime a percentage of speculative operators have wandered into the next most attractive

field of operations, which because of previous good showing for several years past is likely to be city real estate, in the unboomed cities only. This speculators can manage for themselves and it cannot be juggled with. Less capital than one would suppose, is required at this time to start speculation in real estate, as it has already gained the confidence of the people. Investments in lots and houses for home purposes have for some time been fairly heavy and quite satisfactory, so that a considerable activity already exists in this line.

Many who are afraid to invest in bonds turn to real estate mortgages, attracted by the good rate of interest paid by the latter and by the solid character of the collateral offered. This money helps the real estate movement by supplying necessary funds to aid in financing it.

A condition precedent to this speculative movement is a decided fall in interest rates and a surplus of money in the banks, whereas high rents are still maintained, they being the last to decline. The fall in interest rates in this case has the same effect as a rise in rents, causing a marked gain in the percentage of profit paid by realty in comparison with other investments. All other lines having been tried and exhausted, real estate is the last to be taken up. Having steadily risen when other commodities and stocks have fallen, and with a fair supply of idle money at reasonable rates, realty of late has proven a very attractive field to the speculator who inflates values, often in a manner to result disastrously.

As this movement grows it is joined in time by many merchants who have a surplus, and by others that are doing poorly and hope to make outside profits, and still later on, by some of the refugees

from Wall Street. (It is when this boom is over that the public find themselves weighed down with vast obligations which prove to be the hardest of all to liquidate. It is then that the fall in values sets in in real earnest in all lines and becomes excessively burdensome, leading to a rapid exhaustion of resources and ending in panic.)

Land movement.—High prices for their products, with mortgages paid, has superinduced heavy land buying in those Western districts where lands are still cheap. Many of the purchasing farmers borrow of local banks and insurance companies, to assist them in their purchases, so incurring a considerable indebtedness.

In a dull market the element of convertibility is lost.—As the market becomes dull, one great essential of value is seriously impaired, viz., convertibility; and values recede the more easily in proportion as this element of support wanes.

Both jobbers and retailers cautious.—When prices commence to fall, jobbing houses and retailers alike buy as little as possible, in order to avoid losing money by the fall in prices, and in the hope of purchasing cheaper. This is a serious check on production, and is apt to overload the manufacturer with stocks on hand that he finds it hard to get rid of, and eventually sells only by a decided reduction in price or, in some cases, by resorting to the auction mart.

Manufacturer most affected.—The manufacturer is thus affected more than anyone else, for not only does he suffer from the decreased purchasing of consumers, but he has now to carry a larger proportion of finished goods, which requires considerable money. It is no wonder, therefore, that this condi-

tion is now reflected among business failures, the proportion of increase among manufacturers being decidedly the largest.

Indices of liquidation.—Besides the features above mentioned as conducive to a period of liquidation, there are certain indications which point as an index finger to the coming change, a few of which are given below.

Lessened profits.—A narrowing down of the margin of profits indicates overproduction and overcompetition. This feature has been in operation for some time before the fall in values which is now occurring.

Imports.—A gradual falling off in the importation of luxuries. In new, developing countries like the United States, imports will often show an abnormal increase prior to and during the early part of the depression, and will grow much faster than exports until within about three years of the panic. This intensifies the failing times by running us into debt and causing a foreign balance against us. Some mistakenly consider these large imports as a sign of prosperity whereas they are simply an indication of the extravagance of the people.

Solicitation of orders.—The solicitation of new orders should be closely watched for an early indication of poorer times. Unusual eagerness of the producer to secure contracts indicates lessened purchasing and increased competition; later appears a quiet concession in terms and prices.

Buyers holding back.—Another indicator is that buyers are not so anxious to purchase ahead, and now hold back their orders for lower prices. Concessions in price follow, for no combination, how-

ever powerful, can resist the tendency of the period for any great length of time.

Railroads affected before industrials.—Railroad gross earnings may for a short time increase after the top wave of real prosperity has passed, but items constituting expense have so increased owing to dear labor, high interest rates and high cost of materials, that net earnings show a lessened percentage of gain or even a loss. As a rule, they suffer from these conditions before industrial companies do, as the railroads are so much more an object of public attention and criticism that it is very difficult for them to raise their rates. In the long run, however, the railroads, if well managed, keep up a better showing than general business; for finished goods, although a result of overproduction, have to be marketed some time, even if at a loss to the owner, and in many cases old orders are being filled and freight rates paid on them. Besides, the railroads reap the benefit of the efforts of those who try to make up for diminishing profits by doing a larger business. Still later, they are favored by the lower commodity prices and decreased wages. They are also able to practise economies in maintenance of track and equipment and in stopping new construction, resulting in a great reduction in expense account. Again, many merchants are still hopeful, anticipating that each year will usher in better times, endeavoring to do more business and going to expense for that purpose. All this makes freight for the railroads.

Eastern roads show a decline first, as the East is the manufacturing center and manufacturers are at this period more affected than farmers and merchants. Also Eastern roads have been put to a

greater expense per mile than Western to meet the increased traffic. Their terminal improvements and extensions are much more expensive, and are often of a nature that does not yield a profit.

Currency in circulation.—At this time, normally, the volume of currency in circulation should begin to contract, indicating that business is decreasing, so that there is more than money enough on hand to finance the existing volume of trade. But under our present laws contraction of currency is difficult and unused money is likely to accumulate in bank vaults, thus helping materially to reduce interest rates later on.

A quiet withdrawal of national bank notes from circulation indicates a falling off in business, and a consequent calling in of some of the banks' idle circulation.

How labor is affected.—Before a reduction in wages comes first a cessation of overtime work; then, employment in certain lines not being so steady, work gradually ceases to demand the laborer, leaving him to seek work with increasing difficulty, until finally many are not working full time or are even idle.

Better demand for bonds.—A better demand at this time for bonds sold over the bankers' counters, with stocks falling, shows the early stages of a development of fear on the part of the public. This demand grows as the feeling spreads. The public are looking for securities bearing a fixed income, fearing a reduction in stock dividends.

Surplus stocks—empty cars—economies.—A surplus of iron and copper stocks on hand occurs, followed by an overproduction in other lines, due partly to excessive development of manufacturing

facilities and partly to lessening demand. Empty freight cars and an excess of locomotives are now noticed, and a practicing of economies, heretofore disregarded in the rush of boom times, takes place.

Jobber and wholesaler affected after manufacturer.—The jobber and the wholesaler may yet be doing a fair business, while the manufacturer who has overproduced is worrying over the surplus left on his hands; but the former classes enjoy this immunity for a short time only.

Merchants not discounting paper.—Fewer merchants are now discounting their paper or taking advantage of cash discounts. This indicates a shortage of money and poorer collections.

Orders cancelled.—Cancellation of manufacturers' orders is a sign of fast approaching trouble. It is likely to occur first in railroad and then in industrial orders.

Extent of liquidation.—Liquidation must proceed so far that bank surpluses become excessive, and interest rates correspondingly low, before the process is at an end.

Railroads pay up short time notes.—Railroads now, because of their increased borrowing capacity, are enabled gradually to pay up their short time notes, replacing them with long time bonds. This allows them to make absolutely necessary repairs and to settle long standing obligations, and to that extent they help out the business community in general.

Small bills return to banks.—Lessening activity always releases small bills from the tills and pocket books of the middle and poorer classes, as there is less use for them. People are becoming less disposed to spend money. There is, in consequence, a

steady flow of these small bills into the banks from all directions.

Surplus product sets the price.—When overproduction sets in the surplus product exercises an unduly potent influence in establishing the price for the entire output. Overproduction finally forces not only a price but later a wage readjustment. Lower prices are necessary so as to dispose of the excess by enlarging the market, and prices must eventually fall sufficiently to allow this to be done.

First year of decline.—During the first year of the decline the volume of business still remains large (unless a stringency panic occurs to hasten matters) but the results are not satisfactory. The margin of profit has been decreased, the demand greatly lessened, consequently there has not been the usual addition to the wealth of the country. Also plenty of money and easy credit beget speculation in commodities, as wheat, corn, cotton, etc. This induces owners to hold for higher prices; while at the same time increasing bank clearings considerably. During the earlier half of the year, also, the adverse showing is delayed by the filling of old orders, which were taken at profitable rates.

Labor last reduced.—The liquidation must be quite extensive before the great body of employers discharge hands or reduce wages, especially the latter. They do not start doing so, in most cases, until fairly forced to, although when the movement is once under way many who are really making fair profits seize this opportunity to add to them by this means.

Manufacturers hold back orders.—Manufacturers, taking their cue from those who purchase of them, now hold back their orders for raw materials and

labor until the last moment, hoping to buy cheaper, and making a saving in the item of interest, which, to one who carries a large stock, amounts to considerable at the end of the year, especially during a period when small savings have to be enforced.

Liquidation greater in a presidential year.—If this liquidation occurs in a presidential year it is apt to be more intense, owing to the uncertainty as to what policies are to be enforced in the future. A political campaign interferes more or less with business, especially if currency or tariff issues are prominent.

Gold is exported.—When liquidation is fully under way gold is exported to Europe to pay our outstanding debts there, and money later flows from the West to the East, attracted by the interest offered by the New York city banks.

Stocks continue to fall.—Even before the city real estate boom throughout the country commences to wane, and before commodity prices have fallen seriously, a steady decline in stock values has been in progress, which no manipulation can withstand. Later, many of the minor promoters and speculators desert the Street, where there is now very little to be made on either the bull or the bear side of the market, and some of them promote new industrials, such as light and power companies, city railways, and other lines of business, trying to enact there the same rôle they did in Wall Street.

Why there are no great bull leaders.—The reason there are no great leaders to engineer bull campaigns from now on is because so many of the old leaders have left the street, and those that remain have either suffered severe losses or else are overloaded with stocks. They cannot do the one thing necessary to raise prices, viz., buy continuously, and

the public will not help them out, as it never purchases on a stagnant or falling market.

Most news now depressing.—On a receding stock market the news received, and most of the unexpected events that occur from time to time are of an unpleasant nature. The fears of the traders magnify bearish items, and so accustomed are their minds to depressing news, that they become incapable of fully appreciating good news when it comes.

Friction between railroads.—Owing to keen competition, a great deal is heard of friction, strife and ill-will among powerful railroad interests, especially in the West where most of the new mileage is, and where pool agreements and rate associations are at this time apt to go for naught. This factor, however, is lessening of late years because of the many mergers that have taken place and because experience has shown that it has been ruinous in the past

Early signs of decline in realty.—One of the early signs of a decline in the real estate movement is a temporary increase in bank surpluses in the locality of the boom. This shows that less money and credit are being used in the real estate movement. Real estate, unlike stocks, has no bears to sell it short and so lessen the force of the reaction. It lacks, in great measure, that essential element of value—easy convertibility; and hence the liquidating process is a very slow and tedious one and at great loss to the owner.

Money withdrawn from trade.—Much capital is now withdrawn from unprofitable trade channels. The strongest houses are left in control of the greatly lessened markets, and money accumulates in banking centers. Nevertheless, a large expense account (greatly increased in boom times), greed for

money, an innate love of doing, and ignorance of conditions keep many active in business and speculative operations, when prudence should whisper caution and at times even inaction. Some are now driven into speculative lines because of lessened profits or even losses in their regular business, and so incur an indebtedness which weighs heavily upon them later on.

Falling prices and interest rates.—As falling prices always diminish profits or even inflict a loss, there is no inducement for capital to seek investment, and it is allowed to remain idle in the banks at a loss of interest to the owner. As interest rates fall, the value of all securities which bear a fixed rate of interest rises, also of all properties which pay a higher return.

Inducements offered for trade.—When commercial and industrial affairs are growing duller and competition most active, finally, to induce purchases, extended credit facilities are offered by sellers to their customers, and to a much greater extent than is prudent or safe. Eventually this results in a large indebtedness among the merchant class. This has an important effect in bringing on the panic. Such indebtedness bears particularly hard on the small dealer and also leads to excessive loans by the banks to help out their clients. It tends to keep interest too high and cuts down profits, and so has a bad effect on the business situation. We consequently find this condition reflected in the failure list by a gradually increasing number, with smaller liabilities. The small manufacturer feels the effect first and the small trader soon after.

Outside ventures turned into cash.—As the liquidation proceeds many business men turn their outside

ventures and miscellaneous assets into cash and strengthen their bank accounts, and so fortify their business relations.

Another trust forming period.—We are now about to enter a second trust forming period, when divers and often warring interests are consolidated into trusts, in order to reduce the cost of production and of doing business, by reason of larger sales and greater capital, to make a living profit by the practice of wholesale economies, and to put a stop to ruinous rivalry. These combines are defensive in character, giving weak concerns the strength to successfully resist competition; whereas in prosperous times trusts were formed mainly to control the market and were often of an aggressive character, sometimes working harm to their competitors and to the purchasing public.

Fear begins.—Just as on a rising market every one is hopeful, so on a falling market fear is quietly generated, and increases as time passes and values continue to fall. Fear gradually exhausts what we might call the staying power of the people, as well as their financial resources, and eventually ends in collapse.

Farmers hold crops.—As falling prices extend to farm products, there is a disposition on the farmer's part to hold his crops for a time in the hope of better prices. This reacts on many lines of trade—diminishes sales and makes collections slower.

Speculators worst hit.—Falling values naturally have the most immediate and greatest effect on those doing a credit business, and among these the speculative fraternity are the least able to stand a depression; hence it is at first in their ranks that the largest percentage of failures occur. There is also

always a large number of merchants who venture everything on narrow margins, and good times only, when all conditions are favorable, can keep them afloat. These are apt to fail when any severe and prolonged strain is put on the finances of the country.

Europe buys American investments.—As the times become poorer in European countries and idle money fills their banks, they are disposed to invest in gilt-edged American securities, as they pay a better rate of interest than foreign securities—unless they are afraid of our financial condition at the time.

Imports larger than expected.—On the present declining market imports are apt to decrease slower than one would expect (with only a temporary decline if a money stringency occurs). This is because previous high prices have attracted goods here from all over the world and it is difficult to change the inflowing tide so suddenly; also many of the goods were ordered months before, and as European markets also are falling foreigners are anxious to realize on their wares. They may even send goods here to be sold on commission, knowing that their own market is very poor, but not realizing at first how seriously and permanently ours is affected as well.

Also, many Americans who buy foreign goods do not at first realize how serious the situation is, but imagine that it will soon change for the better, and so continue their purchases. They thus avoid for the time being the discomfort and humiliation attending a serious curtailing of their expenses, with consequent loss of social prestige.

Capital timid.—When capital is hampered by uncertainty as to the future, that condition operates as a check on all business operations and prevents the

capitalist from placing his money out on anything like a long time engagement, when events beyond his control might intervene to cause him an ultimate loss. He prefers to take a lower rate of interest and place his capital where it is absolutely safe.

Business large, profits small.—While during this period and before the commercial crisis there are years when the volume of business is large and the situation looks more cheerful, yet on close investigation it will be found that appearances are very deceiving; that the risks of business have been increasing and the percentage of profits quietly decreasing. Appearances, therefore, are at times semi-prosperous, yet real prosperity is not attained. In fact, some country store-keepers find business so unprofitable, owing to the double loss, as it were, entailed first by excessive competition and second by falling values, that they offer to exchange their stocks for realty, in the hope of bettering their condition.

Weaker companies pass dividends.—The first companies to reduce or pass dividends or to pay in script are the weaker ones, whose credit in the money market is poor, and who therefore at this time are often unable to secure funds to pay expenses incurred or to be incurred.

Why imports lessen.—When prices go so low that the addition of freight and tariff to cost makes it unprofitable for foreigners to sell goods in America, imports lesssen and our manufacturers reap the benefit.

Exports increasing.—The ratio of exports to imports now begins to increase, as manufacturers are prepared, by reason of their improved plants, lessened charges for interest, raw material and labor,

and new economies practiced, to manufacture goods at less cost than heretofore.* Prices must eventually go low enough to allow us to compete with the world's products and so finally to pay our debts abroad.

Emigration East to West.—A quiet flow of emigration from the overcrowded East to the partially settled West, with its greater opportunities, is one of the results of the liquidation in operation during this period. Also, much Eastern capital goes West in search of greater activity, where interest rates are higher and profits more promising.

* Burton on Crises, p. 89.

XII.—In the Shadow of the Panic

[NOTE—*These conditions last prevailed in* 1892. *They may naturally be expected to recur about* 1912.]

THE entire period of liquidation up to the time of the panic averages about six years or thereabouts. It was so from 1887 to 1893 and from 1867 to 1873. We are now arrived, in this chapter, at a period about one year before the coming panic, when the shadow of what is to come may be seen by the student of finance; for all great events are preceded by warnings legible to those who can read. We are about to decipher these signs down to the time of the panic.

A brief summary of the past.—In forecasting the future we must remember that each new year is the product of the years preceding it, and to appreciate what is coming we will briefly summarize the past.

"First comes an ascending wave of activity and rising prices, then prices reach a point that checks demand, then comes a period of hesitation and caution, then contraction by lenders and discounters and temporary exhaustion of liquid capital, next a weakening of values, and then holders simultaneously endeavor to realize, and so accelerate a general

fall in prices of stocks and commodities." Credit in business lines becomes more sensitive and is contracted, transactions are diminished, losses are incurred through keen competition and depreciation in values, and finally the ordeal becomes so severe upon the debtor class that forcible liquidation has to be resorted to, and insolvent firms and institutions must be wound up, to begin anew later on perhaps.

Events before a panic.—Small profits and declining wages and credits continue for several years before a commercial panic, together with increasing losses by reason of bad debts, and finally a gradual decrease in activity and production. This latter entails the heaviest loss on the manufacturer, as he not only receives less for his product, but by reason of his not producing to the limit of his capacity his goods are costing him more. This situation doubly impairs the profits of his business, and throws many of the smaller manufacturers into bankruptcy.

Lessened activity in other countries.—Diminishing activity and purchasing power in other countries also, generally precede a commercial panic here.

Panics in some foreign countries.—Panics in some other countries generally occur within a year of the panic in ours. They more often precede ours by a year. This is because of the intimate relations existing between all countries, through the telegraph and cheap and rapid transportation, making, as it were, of all modern nations one big family. Formerly a panic was likely to be limited to the country where the famine or war that brought it on occurred.

Signs of panic years.—In panic years bank loans and discounts reach a maximum and specie a minimum. There is a general drawing in, a tendency to

touch nothing speculative, and collections are slower and grow harder as the panic approaches.

Insufficient money not cause of panic.—An insufficient amount of money in circulation is not the cause of the extended distress, for at this time prices fall rapidly and much money has been released from various undertakings, but is jealously hoarded. Later on, after the panic, interest rates become very low. This is as much due to lack of confidence in the times and the borrowers as to losses in the immediate past.

Banks have often helped on panic.—When we realize that the bank is the headquarters for money and credits, that the banks in the United States have all had to learn their business in a comparatively short period, and that many to-day who branch out as bankers are utterly ignorant of the business or perhaps are speculators who have organized a bank for their own purposes, we are not surprised that some of them have at times been prominent factors in creating a panic. They have often solicited deposits from the people and then placed these deposits where they could not be had when the people wanted them. They have sometimes boomed stocks beyond reason, and then, becoming frightened, have suddenly withdrawn credit to an extent disastrous to business. They have at times issued excessive credits and wild-cat currency. Some bankers regard their banks as mints to issue unlimited currency and credits for their own benefit, instead of as intended to assist trade with judicious loans. Sometimes, after the banker has fostered speculation, he has been the first, later on, to hoard cash in order to save the bank.

These dangerous features, however, are gradually

disappearing. The number and influence of conservative bankers has been growing rapidly of late years, as the experimental stage of American banking passes, and eventually they will doubtless in great measure do away with excessive speculation.

Banks feel the money drain first.—Banks, being the depositories of ready money, which is so much desired when distrust sets in, are the first to feel the drain. Especially is this true of savings banks, which first show a deposit shrinkage (generally one to two years before a commercial panic), because they have a class of depositors who are more easily influenced by fear, and whose needs, also, are the greatest, as their entire income depends, in most cases, on wages, and these are reduced, or in some cases stopped altogether. They have to fall back on the only resources left them, their savings bank deposits. The business man whose capital has been impaired through losses is now found anxiously soliciting loans of the commercial banks and so reducing greatly their balances.

Inflationists active.—Both before and after a panic, inflationists are apt to busy themselves trying to save the nation with their quack nostrums. It was the greenbacker in 1873, and the silverite in 1884 and 1893. A large number of people always think that money is the panacea, and often at the very time when the banks are loaded down with it.

Strikes.—Serious strikes begin about two years before the commercial panic and this condition grows worse until some time after the panic is over. Continued depression at last shows the strikers finally the hopelessness of their efforts at this time, when there are so many workmen idle who stand ready to take the strikers' places.

Trade unions lose members.—Failing times bring into operation among trade unionists the greed, self-interest and necesssities of the individual, as against the demands of his union, and if the depression is great and long continued, vast numbers will desert the unions and look after their own individual interests. Also, the payment of the dues grows burdensome.

Radical changes proposed.—Radical changes in fiscal or economic policies are often proposed as a remedy for stringent money conditions. Such proposals at this time serve only to intensify existing evils and render them still more acute.

Excess of imports a bad feature.—A continued excess of imports over exports, in a debtor country like the United States, indicates danger ahead. We cannot continue permanently to buy more than we sell. (In a creditor country this feature has not the same significance. See Burton on Crises, p. 201.) The decrease in imports is compulsory and is due to diminished consumption or purchasing power.

Wall Street's wealth is promises.—The wealth of Wall Street, its bonds, its stocks and commercial paper, consists of promises to pay, or shares in prospective profits. Raise a doubt as to the solvency of these promises and you upset the financial, commercial and industrial world. Wall Street is the headquarters of all this wealth and of ready money as well, and it forms, therefore, the nerve center of American business.

Lessening bank reserves.—Diminishing bank reserves are an important danger signal before every panic. The time comes when the banks' supply of cash gives way under the mighty strain put upon it by expanded credit. This always generates fright.

The mere fact that cash is running low makes every one want it. Prices decline and paper profits are often supplanted by losses. The seeds of panic were planted in a time of abundant money and credit, and it is the withdrawal and destruction of these that bring on the panic.

Money stringencies necessary.—The government, acting through its officials, has often helped to tide over a money stringency, but its methods have generally been those of further inflation which, in the end, only intensify the depression by furnishing a basis of money with which speculators may continue their operations. The efforts of the banks, also, have frequently had a similar effect.

Money stringencies, under present conditions, are necessary to restore things to the normal, restraining overproduction and overtrading. Such conditions should be, in most cases, allowed to work out their natural course. Measures of relief should be temporary, simply to tide over a crisis without permanently inflating the currency.

Effect of large harvests now.—An abundant harvest now is not enough to avert a panic except for a short time, even though foreign harvests are poor; but such a harvest does alleviate the liquidation afterwards, unless agricultural prices are exceptionally low.

Some producers having a hard time.—Manufacturers who have incurred obligations on the basis of the old inflated prices and have made investments which can be profitable only on a high price level, are now forced to sell goods at a sacrifice, to contract their operations and to reduce wages and working time. Others, with the great fall in prices and

the consequent rise in the value of money, find themselves unable to meet their obligations.

Part railroads have played.—It was in 1830 that railroads first appeared, with about sixteen miles built at the end of that year. It was not until 1845 that they had got fairly under way and were anything of a power in the business world. They have been the great developers of our country, but have been necessarily a disturbing feature as well, as any great, new, untried factor entering into business life must necessarily be at first. The railroad had its excesses to go through, when it was built far in advance of the times, as in 1873. Competitive building, as in 1884 and before, brought ruinous rate wars. Railroad conditions helped largely to bring about the panics in both the above years. Unjust discriminations and high rates were met, in poor times, by granger and even national opposition, expressed in adverse legislation. The general legal status of the railroad, its powers and limitations, had to be established by constant legal strife. At present the railroads, like all other corporations and individuals, are forced to combine their forces and capital in order to meet the demands of modern industrial organization for the production of the best at the lowest price possible. This want can be met only by large capital doing a large business on a basis of small profits. This principle is often reduced to such a fine point that economies in operation and the saving of former waste, pay the profits demanded by capital.

Corporations necessary.—The fact that corporations sometimes abuse their powers is no argument against their existence. They represent the cheapest form of production and distribution. Errors that

grow up may be remedied by legislation and by public opinion, but lawmakers should be careful not to so handicap corporations as to impair their utility.

Fear grows greater.—Gradually the public begins to realize that the country has been deluded with all sorts and varieties of paper evidences of indebtedness or ownership, in the shape of bonds, stocks, construction companies' notes, etc., while extravagance and speculation have crept into all lines of business and into private life. It takes time for the people to realize this, but with diminishing profits and a lessening volume of business, the consciousness finally comes home to them and the feeling of fear grows greater and greater. "The year before a [commercial] panic is apt to be one of apprehension and stringency in the money market; rapid fluctuations on 'change and a downward tendency in stocks; a year of poor business in all lines, a foreshadowing, as it were, of what is to come."

On a declining market the fear that an evil may materialize is very effective, whereas on a rising market it is lightly tossed aside. The seeds of fear germinate best where the soil has been properly prepared.

The people become restless.—The sale of luxuries falls off first, then "necessary luxuries," so called, and finally necessaries. It is at the latter stage, when wages have been reduced that the masses become discontented and all sorts of panaceas are freely aired on the political platform. Ill-advised laws are in danger of passage and the more turbulent at times indulge in violence. It is a hard thing for most people, and an impossible thing for some, to practice close economy and patience, especially if on an empty stomach. This unrest extends to all the

peoples of the civilized world. They want greater political freedom, and if the government is an autocratic one the outlook frequently becomes serious. Governments have often in the past hinted vaguely at great dangers surrounding the nation, in order to secure from the people the desired appropriations or to divert their attention for the time being.

Call for cash shows up weak institutions.—The constant call for cash during this year is apt to show up to bad advantage many of our financial institutions that may have indulged in outside ventures, or that have been ruined by some one of their officials. This year of depression, on the other hand, is not without its benefits, as it stops all branching out and enables many to curtail their purchases and operations and reduce their indebtedness, the burden of which is now felt heavily.*

Government bonds in favor.—At these times banks, trust companies and insurance companies buy United States Government bonds, not only because they are the safest investment, but also because no other class of investment could so effectually strengthen their position, or be so relied upon for immediate use in raising money when suddenly needed.

Credits shrink—Credits continually shrink as losses are made and dishonorable methods exposed in business life. Fear spreads throughout financial circles and money is gradually hoarded, until finally conditions are ripe for the panic.

Immigration.—During the period of depression that precedes the commercial panic the immigration question becomes one of the important features of the day, and is pretty sure to be embodied in some

* See *Financial Chronicle*, Jan. 24, 1874.

form in the political platform of either or both parties. The unemployed are naturally jealous of alien competition, and as the times grow harder, they demand the abrogation or modification of existing laws on this subject, making it harder for the foreigner to enter the country.

Western banks feel strain.—The great demand for money prior to a commercial panic and the consequent strain on the banks, the custodians of money, is felt severely out West among the new banks, whose methods of business are new and more or less untried and have often not been of the best. As these banks now begin to fail confidence is still more shaken in the business centers.

Narrow stock market.—At this period most of the business on the stock exchange is represented by half a dozen favorite issues, which are manipulated by professionals. The public are not interested.

Bank no stronger than its securities.—A bank is no stronger than the securities which back it up, so that when doubt sets in as to the solidity of these, it is apt to extend to the bank that holds them.

Loan increase.—A steady, long continued increase in bank loans occurs at about this time. It is especially serious if attended by a scarcity of specie, and at the same time by diminishing prices. The scarcity of metallic money is in part a result of gold exports. Gold is going abroad to pay debts, as foreigners are worried, and specie is the only money accepted abroad for our debts and in payment for the stocks which foreigners are now sending back to us (as before 1857, 1873 and 1893). Shrinkage in bank reserves and increase in liabilities is an important feature foreshadowing a coming panic at this time.

Call and time money.—Call money very low and

time money correspondingly high and scarce, indicates fear on the part of lenders.

Increase in paper money over specie.—An unusual increase in the percentage of paper money to specie occurs in panic years, not only because foreigners accept only specie in payment, but also because gold is the favorite form of money for hoarding.

Great demand for money.—When many are, as now, trying to get on as near a cash basis as possible in order to be safe, the demand for money becomes at times very great and is quickly reflected in the stock exchange, where the fluctuations are rapid, causing sharp declines in stock values, sometimes verging on panic.

Commodities accumulate.—As the panic comes nearer, commodities which formerly found ready consumption, even though at reduced prices, now accumulate in manufacturers' hands. In some lines auction sales are inaugurated in order to get rid of them, and many are exported, but still the accumulation goes on and the demand quietly lessens.

Events preceding panic.—Falling prices, lack of work, small or no profits or even losses, declining wages; lessened credits, stagnation in stock, commercial and industrial circles, stringent money markets, high interest rates; lack of confidence, rumors of business troubles, gradually becoming more definite, and increasing failures, all precede a great commercial panic. As conditions grow more acute, rumors are afloat in regard to solvent and insolvent firms alike, sometimes even the greatest names in the business and banking world.

Low prices for agricultural products.—The low prices for our agricultural products that generally come at panic periods when all values are falling, not

only reduce the debt-paying power of the producers but the money value of our exports as well, and so act doubly to intensify the bad times.

Bonds go down.—Bonds steadily decline just before a panic while stocks may fluctuate. This is because banks, trust companies, etc., have constantly to sell bonds to get funds to meet the demands of their customers, while stocks are more subject to speculative influences.

Foreign exchange high.—If foreign exchange is high at this time, it indicates that Europe is absorbing our gold, or that exports are small, or both.

Decrease in deposits.—There is a decrease in deposits just before a panic. This decrease would of course be much larger if all deposits consisted of cash, as in the early days of banking; modern deposits mostly represent mere bank credits, and these are often increased before a panic by reason of loans. The borrower receives his loan in the form of a check, which he at once deposits at his own bank.

Talk of booming stocks.—Often, before the panic comes on, certain stocks are heavily manipulated and there is talk of booming them, due probably to an effort on the part of those who are under the load to sell out at the last moment.

Cash and short credits supplant long credits.—When the panic is in sight cash and short credits gradually take the place of long credits, and this continues for some years after the panic. The enormous shrinkage in deposits when the panic is on and thereafter, represents not only the actual withdrawals but also the fading away of these long time credits on the books of the banks.

Dishonest disclosures. — Dishonest disclosures

sweep over the land like a wave of crime just before and just after a panic. This often represents corrupt acts begun some years back, but only coming to light when failure takes place.

Gold in demand.—During and just prior to a commercial panic, so universal is the distrust that many have lost faith in everything but actual cash, gold generally preferred, "not only because it is the measure of all values, but also for the reason that it is the only article in the market that is appreciating." Indeed, at this time the value of gold, as measured by what it will buy, is rising at a most rapid rate, whereas everything else is falling.

Panic started by banks curtailing credits.—The panic is precipitated by the banks curtailing credits and later on enforcing payment of notes and indebtedness of clients whose capital for some time past has been gradually depleted, and who have made their bank borrowings take the place of this lost principal. The banks finally can no longer supply this demand, because of the gloomy outlook and their own overloaded condition. The first signal generally comes by the country banks calling on the New York banks for their balances, which they now need for their own protection or use.

Some large financial institution first to fall.—The first failure before a panic, which usually ushers the panic in as it were, is apt to be some large financial institution with fiduciary features attached, as a well known bank or trust company. Against this institution charges of fraud or speculation are very likely to be made. A disclosure of this description has the greatest and most lasting effect when it reveals a condition which may be more or less general, and is not a mere passing incident. This corporation

is usually in a line of business that requires ready money. It probably has large sums coming due, but it is made vulnerable by having deposits that a frightened public can demand. If it has the additional handicap of a poor or speculative reputation among those who know its standing, such reports will now spread rapidly, and thus intensify the demand on it for cash, and perhaps prevent others from coming to its aid.

Who started previous panics.—"In 1873 the panic was started by a banker who had advanced to a railroad, and could not renew his notes. In 1893 it was a railroad which had bought up other roads and could not meet its obligations. In 1907 it was a copper speculator who got his bank in trouble by trying to corner a copper stock."*

Each panic has its own features.—Each panic has some particular feature, such as wild land speculation in 1837; excessive increase of money circulation and wild-cat banking prior to 1857; overextension of credit in 1866-67; inflation of currency and unwise building of railroads into unproductive country before 1873; free silver agitation and competitive railroad building in 1884; free silver agitation and overissue of silver dollars and certificates before and after 1893.

Runs on banks follow.—This failure is the final blow which upsets all lines of business. A run follows upon banks and other fiduciary institutions, securities are sacrificed first by the victims of the run, then other necessitous holders follow suit, and others still who wish to strengthen their position, until the rush to sell becomes general and finds

* *The Evening Post*, Nov. 9, 1907.

expression in the outbreak of panic, when the public for the time being seem to have parted with their senses in their wild rush for money.

XIII.—The Commercial Panic

[NOTE—*These conditions last occurred in* 1893. *In the natural course of the 20 year cycle, they would be repeated in* 1913. *Of course there can be no certainty that the 20 year period will be exact to the year, but at present writing there is no factor in evidence that would seem likely to cause any wide variation.*]

DEFINITION of panic.—The Century Dictionary defines panic as sudden or groundless fear—"an exaggerated alarm, which takes possession of a trading community on the occurrence of a financial crisis, such as the failure of an important bank or the exposure of a great commercial swindle, inducing a general feeling of distrust and impelling to hasty and violent measures to secure from possible loss, thus often precipitating a general financial disaster which was at first only feared."

Crisis defined.—Crisis is defined as the point of culmination—a critical time—a decisive point. The two words are often used indiscriminately, but panic properly refers to a mental state and crisis to an existing condition; the one disappears but the other remains.

A crisis has its origin in the money market, a panic in the minds of the people. Either one may bring about the other. The crisis comes with the culmination of high prices and the panic is the fierce competitive bidding for money in exchange for goods, securities, or credit. A panic starts with nervousness and often develops into hysteria and frenzy.

Panic results from inflation, speculation and extravagance.—The primary or basic conditions must be unsound to beget a commercial panic. It is the natural result of excessive debt-incurring, inflation, rash speculation and extravagance, which have at length broken down the credit system.

Some of the features leading up to panic, as enumerated by various writers, are as follows: Turning liquid capital into fixed forms; excesssive real estate inflation; wild-cat banking and too rapid formation of new banks; wars; dishonesty and intense desire to get rich quick; too great a volume of business in proportion to capital; too long commercial credits, leading to speculation instead of debt paying; unwise expansion of credits and circulation by banks, or unnecessary hoarding of cash by them and by the people; withdrawals of credits when the financial sky darkens; stoppage of business enterprises caused by fear of shortage of money; too much borrowing of capital at home and abroad; want of confidence; contraction, expansion or debasing of the currency; extravagance, waste and wild speculation; excessive importations; overproduction and overdoing in all lines; inventions destroying existing values and temporarily depriving many of wages; inflation in security and commodity values; fraudulent disclosures in business; railroad and other stock watering incorporations; changes of administration and political

agitation; excessive building of railroads, mills and factories; excessive rise in prices of labor and materials; railroad wars and rate cutting, and price cutting in commodities; distrust setting in, accompanied by a growing desire to get from under the load of debt; excessive output of gold, causing a too rapid enhancement of values.

It will be seen that most of these causes merely represent different phases of the same general condition. Widespread indebtedness, involving overextension of credit by the banks, is the main feature that brings on a panic, and we must, in every case, have a condition of extensive indebtedness before a great panic can occur.

Catastrophe alone not sufficient to bring on panic. —A great catastrophe may induce lower prices, but it can of itself never bring on more than a temporary money stringency or a flurry in general business, unless there is a great existing indebtedness to beget widespread distrust. As an instance, the passage of the Embargo and Non-intercourse act in 1807, though it almost destroyed our foreign commerce, was not sufficient to bring on an actual panic, there being no excessive indebtedness at the time. The great ten million dollar fire in New York City, December, 1835, was not sufficient to bring on a panic or even to cause a cessation of the wild realty boom then on, and because of the rapid rise in prices, to the amazement of all, it did not even cause a failure. Neither Black Friday nor the great Union Pacific corner affected commercial and industrial lines to any important extent. Likewise the San Francisco fire failed to check the great business activity of 1906.

The failure of the great Panama Canal, though it

hurt thousands financially, did not create a panic in France, as it would have done had the shareholders been indebted to banks, instead of having paid for the stock out of their savings.

No commercial panic is possible when business is contracted and on almost a cash basis, when merchants are engaged in no hazardous undertakings and old debts have been mostly liquidated, and when everyone is practising economy, as is the case two or three years after a commercial panic. Any disaster happening then would simply tend to increase the depression—there could be no important recurrence of panic.

Rapidly growing countries suffer most from panic.—To develop natural resources both capital and credit are required. Success leads on naturally to an extension of credit until it is stretched to the limit, and hard times coming on find the borrower unable to pay, as cash, not material resources, is necessary for payment. Hence a rapidly growing country, with vast resources to develop, like the United States, generates far more credit than an older country like France, for example, where the tendency to overproduction and overextension of credit is much less and where exports and imports do not vary so greatly; therefore the former suffers much more frequently and severely from the effects of panic.

We are a young, optimistic, enterprising nation, exhilarated by the great opportunities before us, and we are apt to overdo and to overstrain our credit. Our business methods are as yet not fully established. We are still, to a great extent, in the formative, experimental stage. Also our thirst for capital is keener than that of any other leading nation, as the direct result of our greater resources and the

task of developing them. The more rapid the progress made, the more frequent and acute are these financial crises.

Investment buying in older countries.—Also, in the older countries there is a large and rich investing class, who have money to buy stocks at panic prices, and who loan when money is high, so mitigating to a certain extent the effects of the panic.

East feels panic worst.—In the United States panics start in the East, as it is the money center, and a panic always begins in the financial markets with an urgent demand for money. New York City, being the chief money market, is the first to feel the effects. It is some time, generally a month, before the panic is fully felt on the Pacific Coast. New York City also feels it the worst, though many smaller towns, owing to an insufficient supply of money, may take longer to work out a recovery.

When crisis comes.—Says one writer: "When loanable funds and money seeking investment are absorbed, then the check thereby imposed on further ventures brings on a crisis. Securities and goods accumulate, an appeal to the banks is made (as it is money that is needed), but they are unable to respond (or disinclined through fear). A bargain sale of goods and securities finally ensues in order to get ready cash to pay pressing debts, and a crisis is on, intensified by the widespread feeling of panic that prevails."

Crisis not due to scarcity of money.—Because money is hard to get in a panic, there has often arisen a popular delusion that scarcity of money is the cause of the crisis. In fact, however, there was an abundance of money in 1837, 1857, 1873 and 1893, the *per capita* circulation in each case being above

or near the previous maximum, and there was also a large amount of paper money compared to specie. The crisis is due, not to scarcity of money, but to excess of credit. The banks, previously overloaned, are compelled by the general fright to call in their loans suddenly, and sometimes unadvisedly.

Why recent crises are world-wide.—"Recent crises have been as world-wide as the extension of the modern mechanism of industry and credit, and the spread of the disturbance over a wider area seems to mitigate its severity at a given point." This is due in large measure to cheap and rapid transportation facilities, the telegraph and improved business methods. A surplus in one market is conveyed quickly and cheaply to another where a shortage exists, so that prices are better equalized.

Old wheat prices.—In 1840, one writer says, grain varied 100 per cent. in price between England and Prussia, and a deficiency of one-sixth in the English harvest (which is a frequent occurrence in every grain-growing country) raised prices there from 100 to 200 per cent. Wheat in England in 1243 was 6 s. a bushel, 48 s. in 1246, 72 s. in 1257, and 28 s. in 1286. Before the era of cheap transportation freight on wheat from New York to Buffalo was more than the wheat was worth. It took longer to send a message from Wall Street to Forty-second Street in New York City than it takes now from New York to San Francisco. A crop failure in past centuries often meant starvation; cheap transportation, better banking and business methods, crop rotation, etc., have changed all this.

The civilized world as a partnership.—Now our business relations with the rest of the world are fast assuming many of the phases of a partnership, or

at least a mutuality of interests, so that severe panics or reactions in one country soon find their reflection in others.

It is the money market that is at the basis of all financial operations, and the world's capital becomes every year more readily transferable from one country to another. Hence money market conditions affect all at about the same time. It is easier now for New York to borrow money from Europe and complete the transaction, than it was fifty years ago to borrow it from Philadelphia. Alfred R. Wallace says, "The ties of commerce unite nations alike for good and evil, and render the property of each dependent upon the equal prosperity of all the rest."

Panic features.—When the panic is first on, we pour into the outstretched hands of Europe, at panic prices, our securities and our grain, and we borrow at big interest rates or discounts all the ready money we can get, to help tide over. At this time the universal demand is for money and almost any sacrifice will be made to obtain it.

Disturbance before and after panic.—A point worth noting is "There is a distinct tendency towards the occurrence of a pressure or disturbance almost attaining the magnitude of a crisis at a time both preceding and succeeeding the date of the crisis proper. In several instances the interval, both before and after, has been two years. This presssure usually occurs at the same season of the year as the crisis."*

Panics usually occur in spring or fall.—Panics seldom occur in midsummer, as business is not so active then and the demand for money is therefore less. They generally occur in the spring or fall; in

* Burton on Crises, p. 30.

the spring when the foreign drain of gold is likely to be greatest, and in the fall when there is the largest demand for money to move the crops, and in some years to carry over summer accumulations of manufactured goods.

Some differing features of securities and commercial panics.—In a financial or stock panic the panic itself is the main feature, as the depression following it is short lived and limited in scope; but in a commercial crisis, while the panic is severe, it is but a secondary feature compared with the long and trying depression that sets in thereafter.

The commercial panic affects not only financial markets, but also manufacturing, mining, agriculture, transportation; hence all lines contribute to the list of failures, and their numbers and aggregate liabilities grow for several years thereafter. In the case of the financial panic, the maximum of failures occurs in the first twelve months following and those later on are relatively small; but after a general commercial crisis failures will continue large for a series of years, and will probably reach the largest amount in one of the later years.

First failures.—When the panic starts, the first failures occur mostly through inability to obtain credit or to realize by immediate sales, whereas later on the cause is more apt to be the shrinkage of values and inability to pay because of exhaustion of resources. During the early stages bankers and brokers, and those whose obligations are payable on demand, feel the pinch worst. Bankers are often weighed down by the burden of unsalable stock or bond issues. The banker is the broker in money and credit, and most of his debts are payable on demand; therefore during a panic period he is be-

sieged from all directions, as the demand is for money and ever more money. Brokers also are among the first to succumb, as they have continually to borrow large sums of money and their obligations are payable in cash or short time paper.

Modern business is carried on mostly on borrowed capital, in the form of bills, notes, checks and open accounts. This is credit. It is the business of the banks to issue and discount these evidences of credit, therefore the banks are the storm center of every panic. Less than five per cent. of the banker's business is in cash, and his main customer, the big merchant, uses checks and paper almost entirely in his business. The banker transfers credits. Checks and notes constitute buying power and represent credit, and back of all credit is confidence. Impair confidence and the whole structure falls.

Business houses fall later.—Commercial houses, having a long line of credits to fall back on and being given time on their purchases, do not feel the worst effects of the panic as soon as banks, trust companies and brokers. They therefore do not fail as quickly as the latter, but their turn comes later on.

Farmers feel panic least.—The agricultural classes are little affected by a securities panic, and are slower to feel the effects of a commercial panic than the rest of the country; in fact, they never feel it as badly, and farmers seldom fail. This is because they incur but little indebtedness and their assets are always salable, being food products. As we must live, these are always in demand at some price.

Runs on savings banks.—Before and during a panic depositors start runs on savings banks, but

most of them shortly after return the money to the bank. Some, however, continue to hoard it, seeking out naturally, through heredity perhaps, the hiding places used by their ancestors.*

No money in Wall Street.—It is usually the case that for several days during the height of the panic practically no money is to be had in Wall Street at any rate of interest.

Greatest fall is in securities.—In a panic the greatest fall is in securities, as commodities, being in a less liquid form and not so directly connected with the money market, are not so easily affected and decline more gradually. Stocks bear the brunt of the excitement.

Industrials fall most in panic.—During a panic industrial stocks fall the most (especially the non-dividend payers), as their business is less stable and will feel the depression before the railroads. The greater part of the shrinkage in stocks takes place during a few days of great excitement on 'change. The reason why the fall in stocks at the end of the commercial panic period is not still greater is that for several years previous stocks have been very low. The greatest inflation in stocks ended disastrously several years before, and prices failed to recover their old level. Moreover, they have fallen greatly the year preceding the panic. The stock market has been very quiet, the general public being entirely out and professional speculators being unable to raise sufficient funds to keep up

* It is impossible to form any accurate estimate of the amount of hoarding that goes on before, during and after a panic. Everyone who hoards knows that his act is making matters worse, and he is therefore very secretive about it. Even large capitalists are sometimes suspected of storing up gold or currency when a panic is imminent.

much activity. Hence there is no great indebtedness in Wall Street, as compared with previous years.

Why gilt edge bonds fall.—Gilt edge bonds would probably depreciate but little in panic times were it not for the fact that so many institutions holding them have to fortify their cash accounts by hasty sales. In such periods as this only the best find sale and then at rapidly falling prices. The great fall in such bonds does not usually indicate fear of these securities, but on the contrary, that they are so good that they can be sold in the worst of times, when poorer offerings have no market.

Government bonds fall least.—During a panic there is for a time an almost complete lack of confidence in everything except government bonds. These fall but little and soon recover and advance. Next to these in stability are state and municipal bonds and the inactive securities of solid enterprises in the great financial centers, providing their credit has been excellent in the past.

Security of principal now sought.—The extent of the fall in securities, after the initial shock, naturally depends first on the degree of confidence felt in the security of the principal, the rate of interest cutting but small figure for a time.

Foreign money attracted.—During a panic, when interest rates rapidly advance, foreign money rushes in to be loaned, as it is a natural law that money goes where the rate of interest is highest, providing it can do so safely. This helps end the panic by supplying gold.

English buy.—The English, having closer business relations with us, are apt to be among the first foreigners to buy our bonds and stocks during a panic. The low prices tempt them, and being further re-

moved from the seat of trouble, they generally have a clearer and sounder view of the situation. This buying helps to end the hysterical stage of the panic, as it shows confidence on the part of foreign buyers that the bottom has been reached.

Most people will not buy in a falling market.—It is not human nature to buy on a declining market, therefore prices in panic periods are not sustained, but go greatly below the intrinsic value of the property.

The psychological aspect.—The panic stage would not be so severe if it were not for the psychological effect of violently falling prices on the mind of the speculator. His imagination conjures up the worst that can happen, and in mortal fear of that worst or of some bogie which he has created in his own mind, he becomes panic stricken, and often acts like a madman on that occasion; and the general loss of confidence and depression of sentiment has almost as much effect as the actual market depreciation. At such times some of the excess excitement generated must work off through the muscles or the results to the brain would be serious. Even such a seasoned speculator as Jay Gould, when prices were going against him in a panic and he was losing control of the assets of a big life insurance company, suddenly administered a vigorous kick to a chair opposite him and exclaimed "Wow, wow!" As men become more intellectual and less emotional, this psychological aspect of the panic is likely to grow less important, a change which will eventually work great good.

Who suffer most.—The wage earner and the retailer suffer less during and immediately after a panic than the manufacturer and wholesaler, because

a reduction in prices does not affect them so quickly, and the decline actually benefits those who have fixed incomes or assured salaries.

Material wealth little affected.—The effect of a panic is not as widespread as it first appears; for the material wealth of the country is but little affected (except as it has been previously sunk in permanently unproductive ventures—see John Mills on Credit Cycles). Indeed, as Burton says, "Those countries which seem to suffer most from these disturbances show from decade to decade the greatest increase in wealth and material prosperity." Juglar also says, "Paradoxical as it may seem, the riches of nations can be measured by the violence of the crises which they experience."

Unfilled orders.—Unfilled orders help out bank clearings and wages in a panic year, as compared with the years that follow.

Stock exchanges closed.—Stock exchanges have sometimes closed for a few days in times of panic, in order to give the people time to recover from the influence of the mad fear they are under. Often, however, the closing of the exchange has merely served to intensify the fright.

Clearinghouse certificates.—In recent American panics the banks have relieved the situation by issuing clearinghouse certificates, which circulate as money until the hoarding of money is over, when they are gradually retired.

First indications that panic is lessening.—The cessation of the intense demand for money is the first indication that the panic is ending, but confidence will not be restored for some time thereafter. The reign of terror ceases, but confidence, on which credit is based, is slow to revive.

Effect of high money rate.—"In panicky times the demand on the banks for loans and discounts compels bankers to raise the discount rate; this diminishes the demand for credit from those who can do without; the high rate attracts capital abroad and locally as well, and prevents also the calling in of many loans which are continued at higher rates, and so helps out the crisis considerably. After the acute stage has passed, the demand for credit, because of the arrested activity and the want of good collateral, declines to a minimum, resulting in a great reduction of loans and discounts, while the diminished demand for currrency sends it back to the solvent banks, and results in the rapid piling up of specie in their reserves."*

Gold imports a turning point.—Gold imports mark generally the turning point in the panic. The high money rates and the small premium on gold or currency which usually appears at this time, enable the banks to borrow gold in Europe. After this comes a falling off in the demand for this European gold; indicating that the situation is now being controlled and that the worst is over.

Disposition now to do little or no business.—During a panic and for some time thereafter, there is a strong disposition to do as little business as possible, and to reduce indebtednesss as rapidly as may be.

* Chas. A. Conant, *Yale Review,* Vol. 9.

XIV—Depression Following Commercial Panic

Covering About Three Years After the Panic, and Including the End of Liquidation.

[NOTE.—*These conditions last prevailed in* 1893-1896. *If the next commercial panic occurs in* 1913, *for example, they would be substantially repeated about* 1913-1916.]

THE depression is that part of the twenty year period after the panic, when a long period of adjustment sets in, when lowest prices are reached and resources are husbanded, so paving the way for better conditions later on. In general, this is a period of gloom, yet a necesssary stage, leading up finally to the convalescence of the patient.

Money in actual circulation shows activity of business.—It is the amount of money in circulation, and not the amount in banks, that shows whether business is active or otherwise. After a panic money soon becomes abundant but everyone is too timid to use or loan it, hence it remains stored up idle in the

banks. There is a shrinkage of values, a diminution of the use of money, stagnation in trade, decline in manufactured output, and intense endeavors on the part of business men generally to make both ends meet.

Falling off in imports.—A rapid decline in imports takes place as the people practice economies in expenditures. Prices fall in all lines, so that importations of many articles become unprofitable. What makes the falling off in imports seem even greater is that a fall in values abroad takes place at the same time. Hence even the same quantity of imports represents less money.

Gilt edge bonds.—The principal investments for a while are those which have withstood the panic best, as United States Government, state, municipal and some other gilt edge bonds, on which the owner can borrow money as he may need it. The small demand that exists for bonds at first comes from the banks, trust and insurance companies, estates and cautious investors, these being the main sources of ready money. Most individuals need their money in their business or are too poor to have any surplus, or have so little and are so ignorant on the subject of investment that they prefer to place it in savings banks to be invested for them. Some are so badly frightened that they trust no one and even hide their money.

The bonds of cities have generally only a local demand, and are therefore not as much favored by the outside public as government bonds. The same applies in a lessened measure to state bonds. The bonds of the best and most favorably known states and municipalities fall less, and are later on more

eagerly sought after than of those not so well known.

Government bonds first to rise.—United States Government bonds are the first to rise after the panic. The high price and small interest return are for a while but little considered by purchasers, as they still look principally to safety of principal.

Governments go through same paying up period.—The United States Government, states, cities, counties, corporations and individuals, all alike go through the same paying up period after a commercial panic. All this reduces credits and so releases money for general circulation.

Protests against taxes.—An indication that the shoe pinches now is found in protests against high taxes which were increased in boom times and were cheerfully borne then, when realty prices were moving upwards, but which for some time past, with declining values, have been a burden.

Social unrest.—During the period of depression before and after the commercial panic, the world's rulers are kept awake nights with the burning questions of the hour, and the people are demanding greater rights. In America, as the people themselves are the ruling power, the position of the government is not so precarious. The unrest takes more the form of antagonism toward the excessively rich capitalist and his corporate enterprises. These agitations, while in the long run evolving much that is good, undoubtedly tend at the moment to intensify existing conditions. Strikes also, on a falling market, act in the same way, and often bring out some of the worst phases of human nature. They are seldom successful at this time, leaving both employer and

employee in worse shape than before to meet the depressing conditions.

Small business in Wall Street.—Brokers and traders complain that the public now takes no interest in Wall Street; yet everywhere and at all times professionals are publicly predicting all manner of evil happenings. Some one with courage starts an incipient bull movement and everyone else immmediately sells short and yells "Panic." Still they complain that the stock market remains dull. The public is seized with a condition of nervous indecision and is content to do nothing. Prices go below intrinsic values owing to an almost entire absence of purchasers and speculators. Securities susceptible of easy conversion and those which retain their market values the best are about the only ones purchased by the public.

Pig iron.—The production of pig iron may show a small increase just after a panic. If so, it is the result of filling old orders, and does not come from new ones. The amount of new orders received is the better indicator of the times.

Exports increase.—Early in the depression our exports increase, first because of the decreased purchasing power of our people and the sale of what we have on hand abroad at bargain prices. Later the increase is due to still lower prices and enlarged output—the fruitage of economy, enlarged manufacturing facilities, lessened wages, and the enormous natural wealth at our disposal. Inventive genius is also at work reducing costs, and labor, after futile strikes, is much more tractable and efficient. All these factors, backed up by dire necessity, open up to us foreign markets that we had thought were hopelessly closed against us. This enables us in

time not only to pay up our European debts, but eventually to become the creditor ourselves.

Mercantile failures.—Mercantile houses begin to fail in great numbers about two weeks after the panic. Comparatively few fail before then, being those who happen to have, at that time, urgent calls for ready money. The constant rise in values during boom years enabled the half-insolvent debtor to extend his liabilities from year to year on the strength of the showing he could make by the aid of the rise, while still increasing his volume of indebtedness. When this support is removed and prices begin to fall, the decline soon dissipates his equity, and he finds himself leading the list of newly fledged bankrupts.

When most failures.—If the crisis itself were the most important event, as in the securities or financial panic, the greatest number of failures would occur then, but when the depression is the most important, as in all commercial panics, the failures are large for some years and reach the maximum in from three to five years—as after 1873, in 1878, and after 1893, in 1896.

Assets realized.—The percentage of assets realized from firms that fail two or three years after the panic is less than from those that fail during the panic year. The former have held on until the last moment and have graduallly exhausted their resources, and often a species of dry rot, as it were, has set in; whereas the latter, having outstanding obligations to meet that called for immediate payment, were compelled to fail while still owning assets which later could be realized upon. Those who fail later have exhausted this fund by the time they

assign. Many of those who fail in panic times are able to resume if dealt with leniently.

Interest rates fall when fear lessened.—When the demands of the necessitous after a panic have been satisfied or refused, money accumulates in the banks and interest rates fall correspondingly; not at once, but as soon as the great fear has lessened.

Some of the hoarded money now spent.—The first money that comes from hiding after a depression, and when measures have been taken by banks to prevent further hoarding, is the money actually expended for necessaries and overdue bills which must be paid in cash. The actual depositing in banks of surplus hoarded cash does not take place till later, when confidence is more fully established.

Prices still falling.—After a panic values still fall in many lines so that merchants continue to incur losses, hoping always for the time when they can do business on a safe, conservative basis. This time will not come until values reach their bottom level, expenses are cut to a minimum and frugal habits established. In the meantime it is a case of the survival of the fittest. The weaker drop out one by one and terminate their careers in the bankruptcy court or in financial oblivion.

Raw materials fall most.—Raw materials now fall more in proportion than manufactured articles. The products of the soil, mines and forests have had the greatest rise, and are, moreover, less affected by combinations and trade agreements and so lack this supporting element. However, the tendency, even in natural resources, is toward larger ownership by constantly decreasing numbers of persons.

Which stocks suffer most.—The highly speculative stocks, which in boom times were active favorites

on the Stock Exchange, suffer more severely during and after the panic than those that have not been manipulated so extensively. Non-interest-bearing stocks are, naturally, among the first to fall, go the lowest, and are the last to rise.

Railroad earnings keep up better than industrial.—The railroads maintain their earnings better than industrials, as some manufacturers endeavor to enlarge their output in order to make up for deficiency in profits, part of their goods being, in many cases, shipped abroad. Moreover, there is a rush after a panic to realize cash at any price, and this also involves transportation. Thus tonnage was larger in the panic year 1893 than in 1892. A year after the panic the railroads begin to feel its full effects, as it takes some little time for business to subside to the lowest level and so react fully on these great highways of transportation, which represent in their yearly business the volume of freight and passengers transported during the year.

Railroads curtail expenses.—Railroads now curtail expenses and reconstruction and so fortify their position. Absorption of some of the weaker lines usually takes place. Their high interest bearing obligations are refunded at lower interest, fixed charges are scaled down, and speculative managements are succeeded by more conservative ones. Later on, aided by large tonnage from the crops and by gradually increased business, they are slowly lifted out of their unhappy condition.

Imagination conjures up many fears.—In times of severe depression the people go to extremes and imagine that the existing unfavorable conditions will continue indefinitely and even develop into still worse; that production is steadily increasing over

consumption, and that other bad features are acting more adversely than is really the case. Consequently prices drop abnormally—a barometer, as it were, of the fears of the public, rather than of actual conditions.

People hold on to their money.—For some time the people choose to do nothing, after their surfeit of speculation, rather than run the risk of doing wrong. Those who have money now hold on to it with the grasp of anxiety and distrust, imagining in almost every proposition offered a scheme to part them from their precious belongings. Better to leave their money idle in the bank or vault, they think, than to venture it in such financial weather. It is not until considerably later, when the bell wethers in finance have ventured out and are undeniably making money, that the masses acquire courage enough to follow their example.

Business on cash basis.—After the panic, as credit is partially destroyed, business has to get as near to a cash basis as is possible under modern methods. It is only after some little time, when the fright is over and values cease falling, and when business men know to whom it is safe to extend credit, that credit begins to enlarge. This movement is slow at first, especially as many prefer, because of small margin of profit, to do less business and avail themselves of cash discounts.

Idle fund sign of stagnation.—The plethora of funds on deposit is now an indication of suspended industry and a barometer of the times. We are likely to loan to Europe at this time, as interest rates there may be higher; and this, with debt paying and taking back our securities, causes gold to be exported.

We pay up foreign debts and take back our stocks.—When a debtor finds it hard to pay a creditor, the creditor is apt to lose confidence in the debtor. After a panic, Europe as the creditor demands a speedy settlement before doing any more business with us. There follows a period of paying up our foreign debts and taking back our stocks from abroad. This continues through exports of gold and merchandise until the indebtedness is settled and a large credit balance accumulates in our favor, putting us finally on a solid basis once again.

People working hard.—The people now settle down to hard work in earnest to make up for the losses sustained or debts incurred. We are constantly studying now how to make our expenditures less and our money and efforts more productive. Overstocks are greatly reduced, even below what they should be; extravagant expenses in living and in business are within bounds; wages are universally lowered, prices of raw material cut, and cost of production in all its elements reduced, to enable business to be done with as many chances as possible in its favor.

Expensive houses vacated.—At this time many of the finer houses are closed or offered for sale cheap, and their occupants sojourn in boardinghouses, which now increase and multiply, though often not on a living basis. The numbers of such boardinghouses is increased by many owners of homes who now take in boarders in order to augment their slender means, but too frequently this merely prolongs their worries until the mortgage is finally foreclosed.

Back to the land.—The source of all wealth is Mother Earth, so back we go at an early period of the depression, to the tilling of the soil, working in

mines and forests, and at the fisheries, to recuperate our wasted fortunes and rebuild the sub-strata for another upward movement in the future, producing raw materials cheaper than before and thus cheapening manufactures, opening up a foreign market, and gradually increasing home consumption by reason of low prices. There is and has been for some time past a quiet but steady flow of population from the city to the land.

Depression helps people the West.—The depression attending a commercial panic increases emigration from East to West. In 1873 it peopled the country west of the Missouri, and in 1893 added vastly to the number of farmers about Omaha and in the far Northwest. The East, being the manufacturing and business center, has no employment for many of its people, so they go West, where the natural resources are the fountain of all wealth.

Rally from panic.—A year or two after the panic there is a short rally, which is greater than is justified, and raises the hopes of the masses; but hopes will not change actual conditions and depression soon assumes full control again. After a panic many entertain the erroneous idea that all that is necessary to restore business to a paying basis is the restoration of confidence; but finally they realize that confidence does not pay debts, but that every dollar has to be earned, while their living expenses continue, and that the readjustment, though long and irksome, must run its regular course.

Legal measures.—After the panic, if there has been legislation which helped to bring it on or to intensify the depression, laws are likely to be passed, after long and tedious delays, to remedy the same; but, unfortunately, not content with this, legislators are

apt to go further and endeavor by passing other laws to help out the situation. Most such laws are framed in ignorance, and the majority of them fail of passage. The state legislatures being smaller and less deliberate bodies than the national Congress, and often ignorant or swayed by passion, are more apt to enact hasty laws which leave a depressing influence. The mere discussion of many of these measures in Congress or in state legislatures retards financial recovery.

A new political party.—The birth of a radical party (or a great growth in some such existing party) is an event likely to take place some time before this period, but it does not receive sufficient encouragement to be a really serious menace to the public welfare, until later, when it is joined by many of the farmers, now thoroughly discontented with their lot because of low prices for their farm products. If not satisfied with the platform of this party, the farmers may form one of their own.

Bankruptcy law passed.—Some time after the commercial panic a bankruptcy law is generally passed, if not already in existence, to allow the financial wrecks to clear up their records and start anew.

Plenty of idle money.—During a depression money is plenty, owing to a cessation of all but absolutely necessary work and the consequent partial stagnation in all lines of business. Again Western bank money seeks New York City banks, in order to get the small rate of interest paid on out of town bank deposits. An increase in savings bank deposits in poor times is not a positive indication of the betterment of the working classes, for some of it is money that in better times would be invested so as to bring in a higher return.

Wreckage being cleared away.—Bank clearings, of course, show less business done; yet the times are really improving, inasmuch as the wreckage is being cleared away, and we are no longer leaning on crippled banks for support.

Money begins to find its way to Wall Street.—When bank deposits increase so that they become fairly burdensome, interest rates go still lower, and money begins to seek Wall Street owing to the decidedly better returns on stocks and bonds than in business ventures. Later, these moneys help to raise the price of Wall Street securities, but too many safe deposit vaults still hold worthless stocks and bonds and other evidences of speculation, for the times to improve much as yet.

How long dull market lasts.—When prices are high a dull market is not apt to last long, but when it comes at the end of a long decline it may seem almost interminable. In the former case the rise has enriched the owners of securities and they are in a position to do business, but the decline has entailed heavy losses and has curtailed credits, so that the dullness is of long duration at this time.

Capital not ready to act yet.—As long as the country is loaded down with an incubus of bad debts and rottenness in firms and corporations continues to develop, brought over as a heritage from the panic year and augmented by the subsequent depresssion, capital is in a state of suspense and timidity. The fearful investor will not place his money on any sort of time engagement when unfavorable legislation, an attack on the soundness of the currrency, a threatened or actual war, or other causes which might at any time loom up before him, would work him a loss.

Any future tinged with doubt and uncertainty

acts as a check on business enterprise, especially the placing of capital in permanent investments, which is so necesssary to the return of prosperous times. The labor strikes attending the depression must be eliminated before a decided improvement takes place and the unpleasant disclosures attending the panic must become a thing of the past.

Competition now active.—Railroads are hauling freight at a very small profit in order to keep busy, doing as all are now doing in an endeavor to increase their profits or save themselves from loss by transacting a large business even though at low rates. Competition is active and later is made more so by the accumulation of idle capital trying to earn even a small rate of interest.

Agreements to restrict output now futile.—Attempts by individuals or corporations to sustain unnatural prices by agreements to restrict production are self defeating at this time, for the tendency of capital is to favor the enterprises that are strong enough to sustain themselves against the world.

Coming of good times may be delayed.—When general conditions are favorable to a rise, the advent of good times may yet be deferred by the fear of unwise financial tinkering of the laws, or by demands of one of the great political parties that might lead to an unsettling of values.

A trying period.—The completion of liquidation after a panic is marked by dull business, steady prices, and a great increase in bank surplus. It is at this period, in the very last stages of the depression, that the times are hardest upon the business man, and it causes the heaviest drain on his already lessened capital and his patience. It has been a slow and tedious liquidation, especially to many

who have lived too long the life of spendthrift heirs to make the process a pleasing one, however healthy and necessary it may be.

Why large crops and mineral output now.—Several years after the panic, so many have gone into developing the country's natural resources and have worked so hard at it that the result is apt to be large crops and a great output of minerals and other raw materials.

Purchasing power of people increased.—During the latter part of the hard times the purchasing power of the people is gradually increasing, and far more than one thinks. This continues for a long time thereafter. The lowest period of the depression, to the unobservant eye, appears to last several years before there is any visible sign of improvement. As a matter of fact, however, the period is much shorter than this. Natural forces soon cause either an advance or a further recession, abhorring a period of inaction almost as much as nature abhors a vacuum.

Savings banks.—During the depressed times before and after a commercial panic the prices of bonds and choice stocks fall to a level that enables savings banks to buy advantageously. Then after the recovery gets under way, the banks can increase their rate of interest, and this helps to draw money from hiding places. Such purchases often afford the bond market support at a time when it is very acceptable.

Railroad bonds finally inspire confidence.—As the process of foreclosure, liquidation and substitution of lower interest bearing bonds nears its end, railroad securities, the bonds particularly at first, gradually inspire more confidence in financial circles. It is the old, tried, well-known issues that are wanted

at this time, and no new issues can be floated unless they are unquestionable first liens on the best roads. The successful flotation of new issues marks a period of returning confidence and shows that the crisis feature is over and the depression is passing away. Both banks and investors grow less cautious in their selections as the supply of money keeps piling up, and as good securities are gradually taken out of the market and transferred to the strong boxes of the purchasers.

Returning confidence.—Money piling up in the banks instead of going into use, indicates an abnormal condition—that fear still reigns in place of confidence; but the accretion of funds steadily continues until confidence gradually asserts its sway. The growth of confidence naturallly depends on the force of the shock it previously sustained, and on the various surrounding conditions, favorable and unfavorable. But the knowledge that such great sums are accumulating in the banks of the country is an important factor in restoring confidence. Such an accumulation of money acts as an object lesson and tends ultimately to cheapen the value of money, depriving it of the false estimate that has been put on it for some time past. Finally it becomes necessary for the owners of this capital to get an interest return, and the money gradually begins to circulate in businesss channels and thus to start up better times. So again an extreme cures itself. Loans and discounts are the best indices at this time of the return of confidence, and they form at all times the best barometer of mercantile activity.

Duration of depression.—The depression that follows a securities panic is generally light and lasts only about a year, but that following a commercial

panic is far more severe and lasts from four to six years. The greater the depression and the longer continued, if the result of ordinary causes, the greater finally will be the reaction; for it is during this time that savings are accumulating, and the larger this fund becomes the larger is the amount to draw upon when prosperity starts, and consequently the greater the boom that follows.

Production checked and decline stopped.—Prices have, in some industries, fallen to the average cost of production or even below, and in all cases the profit is now small. This has diminished production and checked the decline, and marks the end of the liquidation. The number of failures is still large, but the liabilities are growing smaller. This indicates that liquidation has reached the point where those financially well fortified are producing cheaper and marketing at less cost than their small competitors, and that the trouble is now mostly confined to these latter, whose insufficient capital is a severe handicap and does not allow them to do a sufficient volume of business at the lessened rate of profit to make their business pay. They are unable to take advantage of the many little savings that a larger concern can put into operation; so that, while the large manufacturers and wholesalers are first to feel improving conditions, the small manufacturers and dealers are often still *in extremis*.

When lowest point may be expected.—The lowest point of the depression is usually in June or July, when most business lines would naturally be most affected by the approaching midsummer dullness.

Confidence returns when once bottom is reached.—Much capital remains idle and dividends diminished or discontinued until the liquidation has been

thorough and business is mostly down to a cash basis, with short time credits, economy in management, investments strictly non-speculative and on an interest basis, new enterprises almost eliminated, and prices so low as to meet the necessities of the consumer and so create a market. At length nearly everyone becomes satisfied that the bottom has been reached, and from then on confidence gradually grows and forms the basis of new credits; for there is nothing that will undermine confidence, and hence credit, like falling values.

When to buy.—One writer has said that the time to buy is when the decline caused by a panic has produced such liquidation that loans and discounts, after steady and long continued diminution, either become stationary for a period or begin to increase progressively, coincident with a steady increase in available funds. It is this period in the stage of progression that we have now reached, when the bottom has been touched and the tendency, though often so slow as not to be realized, turns upward.

First year of betterment.—The year that shows the greatest number of failures is the period when the first signs of betterment are noticeable—it is the clearing up of the atmosphere after the storm.

Even low interest rates attract idle capital.—When the masses are satisfied that the bottom has been reached (for there can be no hope of recovery until faith in the permanence of values can be re-established), even a low rate of interest serves to attract capital and to start enterprises that can now be made to pay, even at low prices; for interest, wages and raw materials are all corrrespondingly cheap. and the population which represents the demand is in-

creasing much faster than is allowed for by the producer.

A slow rise in prices.—Production has now fallen below what is sufficient to keep up with the increase in population. After this condition has existed for some little time, surplus stocks become thoroughly exhausted and competition in demand causes the first rise in prices. This soon induces greater production, and finally the increasing demand makes new investments attractive. Until this rise in prices takes place the average merchant does not feel any decidedly beneficial effects from the changing conditions.

Europe sells back to us our best stocks and bonds.—Tempted later by higher prices, Europe now returns to us some of our choicest bonds and stocks, and so delays the inflow of gold into this country for some time after one would naturally expect it to flow toward our shores.

It has taken up to the present time for us to pay up our European obligations and to have an accumulating surplus there to our credit. The process has been long and tedious and has needed some good crops to help out; but until this has taken place, no real prosperity can be expected, as our surplus capital, instead of being used at home, is being diverted abroad.

Increase in purchasing.—The period of limiting one's purchases to less than one's needs, let alone his desires, is passing away, and long felt wants now begin to find expression in increased purchases. The years of enforced economy and hesitation are passing.

A land movement now.—Towards the end of the depresssed period, about the third or fourth year after the panic, and especially if the previous year

has seen a good crop and good prices, a land buying movement of large proportions will set in, due to the fact that the farmer has suffered less than any other class, to the increase in population, and to the fact that dull business in the cities has driven many back to the land. Land has paid the best of all investments and farmers have suffered the least. The saving habits of the farmer, now long enforced, with a fairly good price for his crops, have made him well to do and have given him a balance in the bank. This he naturally puts back into the land, for the benefit, often, of his children, who have increased in number, and some of whom have reached an age where they need more land to cultivate. Also, a number of the younger generation have themselves saved up enough to make first payments on account of land purchases.

Recovery slow.—The recovery of the business world from its long period of depression is like that of a sick man from the effects of a severe illness. It is slow and tedious and there are times when reactions set in that for a while dash the sanguine hopes of the patient and his friends. But while slow it is sure, and the rising sun of prosperity finally floods the land with its brightness.

People live on higher plane.—In each new period of prosperity the people reach a higher plane of consumption and enjoyment than ever before.

We have gone through the changes of the twenty year cycle, with its good and bad times, and have now caught up to the period mentioned in the first chapter of this book.

Panic features lessening.—It is difficult at present to forecast how severe the next panic will be, owing to the 1907 panic having occurred—an experience we

did not have prior to other commercial panics; but there is no doubt that in time the panic feature will be practically eliminated, and the depression that follows greatly mitigated. In fact, this has already occurred in the case of the financial panic, for 1903 was nothing like as severe as 1884.

Superior business and banking methods; the rapid development of our country's resources, passing from a speculative to an investment basis; the great accumulations of capital and the growth of a large investment class; better transportation facilities and growing solidity of our railroads, which are now past the experimental and competitive stage; the lessening of adverse and purely theoretical legislation which is bound to come; the abandonment of schemes of inflation or unwise tampering with the currency, and the passage of necessary laws regulating our banking and circulation systems; and our better handling of the situation when the crisis is on, as a result of past experience—all these factors will work together to modify the effects of future panics and depressions.

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